PRESENT-DAY NON-MARXIST POLITICAL ECONOMY

A Critical Analysis

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TO THE FOREIGN READER

The discriminating reader will note that in criticising present-day non-Marxist political economy, we do not take any standard attitude to bourgeois economists, but draw a distinction between the conservatives, who have not learned or understood anything and stubbornly believe that the course of history can be reversed and that the system which is doomed can be preserved, on the one hand, and those who have realised that the ongoing changes are inevitable and seek to adapt to the new situation in the world, which is determined by the development of the revolutionary process and the break-up of the obsolete relations of production.

In this book we suggest that the crisis of bourgeois economics is characterised not only by a failure of its doctrines, which history has invalidated, but also by a quest for new doctrines.

In our day, when there is no alternative to the peaceful coexistence of states with different social systems, a dialogue between economic thinkers of every trend has never been more necessary, for it could help to elaborate common principles in tackling the problems facing the whole of mankind, namely, ending the arms race and preserving the environment. Our day has brought out the abiding importance of the brilliant foresight of Marx and Engels, who adopted as the starting point for their scientific studies the abstract category of mankind as a whole. On thestrength of Darwin's theory of evolution, they established that at a definite stage of anthropogenesis mankind comes to be crucially influenced by social conditions. Its ascent from lower to higher forms takes the form of a transition from the primitive-communal system to the slave-holding formation, feudalism, capitalism, and communism.

In the lifetime of Marx and Engels, communism was no more than a vision. It was Marx who in his immortal *Capital* transformed socialism, once a utopia, into a science and demonstrated in theory that the advent of the communist formation was inevitable. That work also contains a constructive critique of bourgeois political economy and sets out the scientific theory which expresses the interests of the working class, whose mission is to bring about the revolutionary overthrow of capitalism and to build a classless society.

Marxism is not only a theoretical expression of the interests of the working class, but also a summing up of the advances made in the natural and social sciences in the course of mankind's spiritual development.

That is why the Great October Socialist Revolution, led by Lenin, who brilliantly developed the theory of Marx and Engels, was the first truly epoch-making revolution that had a crucial impact on the subsequent development of the whole of mankind, a fact that even bourgeois ideologists have had to admit.

Marxism is now the theoretical expression of the true interests of all the revolutionary forces of our epoch. It has been steadily winning over the minds of progressive men and women on every continent as the most important spiritual component of the modern civilisation.

That is why we hope this book with its promising title will find thoughtful readers in foreign countries who will correctly understand our ideological and humanistic aspirations.

FOREWORD

The crisis processes in present-day bourgeois economics reflect the new stage in the aggravation of capitalist society's contradictions to which bourgeois economic theory seeks to adapt itself.

When we say "present-day", we do not at all seek to confine our analysis to the narrow chronological framework of the current period, but rather use this term to emphasise the urgency and importance of the problems we consider, for they are deeply rooted in the past and largely determine the position of capitalism as a society without a future. We have sought to follow the Marxist-Leninist principle of historicism in political economy, which says that one has to establish the historical origins of every new phenomenon so as to determine its future, i.e. the tendencies of its further development. We have also given considerable attention both to the retrospective and the prognostic approach in analysing the concepts of bourgeois economics we criticise.

The structure of this book has been determined by the logic of our analysis.

The *Introduction* contains an analysis of the present stage in the crisis of bourgeois economics and characterises the prerequisites of its origination, its specific features and development tendencies. It gives a critique of bourgeois concepts of this crisis, which seek to put an apologetic gloss on it.

The present stage in the crisis of bourgeois economics is expressed in two main forms: the bankruptcy of its traditional theories, and the quest for new conceptions of state-monopoly capitalism.

Accordingly, *Part One* contains an analysis of the crisis processes in the traditional trends of bourgeois economics (the Keynesian and the neoclassical), processes engendered by the failure of their recommendations both in implementing programmes for long-term economic growth, and in the sphere of anti-cyclical policy. It also gives the Marxist interpretation of the new stage in the "anti-marginalist revolution", in the course of which bourgeois (especially radical) economists criticise the neoclassical theory. We regard the infighting between the schools of bourgeois economics as an important sign of its disintegration, and also of a growing trend towards radicalisation. Finally, we examine the theories of the monetary crisis rocking the economy of the capitalist countries, and the Keynesian and neoclassical recipes for restabilising the monetary systems and restoring the monetary equilibrium of the world capitalist economy.

Part Two analyses the search for new doctrines and conceptions of capitalism's economic development. This has tended towards ever closer coalescence between bourgeois economics and sociology, involving attempts to counter Marxism-Leninism with a more "integral" and flexible apologetic theory presenting economic and social processes in a single complex. This has entailed a revival and modernisation of the socio-institutional trend and the elaboration of "industrial society" theories and models for a reformist resolution of class conflicts in a "postindustrial society". There is also an evaluation of radical economics, whose individual trends, inclined to recognise the correctness of some Marxist propositions, fall outside the framework of the officially accepted academic bourgeois economics.

The *Conclusion* (Chapter 14) shows how the processes unfolding outside the orbit of capitalist domination and its inherent economic uniformities tend to influence the crisis of bourgeois economics. These are factors behind the development of the general crisis of capitalism which spring from the economic competition between the two systems and the development of the world revolutionary process, an area in which bourgeois economics is invalidated not only by the logic of ideas but also by the logic of events, that is, by concrete historical development. This depends both on objective and subjective factors, such as the class struggle and the role of the parties and masses involved, and the uniformities of social development not only in individual capitalist countries, but also throughout the whole modern world, which is divided into two antagonistic systems.

We cannot, of course, claim to have produced a comprehensive critique of all the schools and trends in bourgeois economics, but we shall feel that we have done our duty if this book helps to stimulate interest in research in this field.

Introduction: THE PRESENT STAGE IN THE CRISIS OF BOURGEOIS ECONOMICS

Bourgeois economics is that part of the ideological superstructure of capitalist society which is most closely connected with its basis. In the period when capitalism was a progressive social system and when its ideologists fought against feudalism, bourgeois economics sought to gain a scientific cognition of reality and did not try to obscure the capitalist system's class contradictions. Adam Smith and David Ricardo, its classics, produced a theory which became one of the sources of Marxism. They not only brought out the objective nature of the economic laws governing the development of capitalism, but also elaborated a theory of economic policy promoting the development of capitalist relations of production as these were established in place of the feudal order.

Bourgeois economics represents the interests and ideology of the capitalist social system and defends its positions in the struggle against the communist formation.

This formation, still in the making, exerts a crucial influence, even in the first phase of its development, on the worldwide historical process of transition from capitalism to socialism, which is the cardinal content of our epoch. Today, more than ever before, bourgeois economics seeks to find ways of camouflaging the objective contradictions of capitalism, instead of giving a scientific analysis of these. It has an even greater role to play not only in elaborating the apologetic theory, but also in applying it in practice and formulating recommendations for government economic policy.

The present stage in the crisis of bourgeois political economy was ushered in above all by the failure of its recommendations designed to substantiate a policy of state-monopoly regulation of the economy. These recommendations are designed to ensure its long-term growth and to rid it of deep-going cyclical upheavals. The irrelevance of these recommendations has been clearly brought out by the rapid growth of inflation since the end of the 1960s and by the 1974-75 cyclical crisis of overproduction.

What was unusual about the 1974-75 world economic crisis was that it was interwoven with monetary, energy, raw material, food, and ecological crises, and demonstrated not only the profound disruptions in the mechanism of cyclical reproduction of social capital, but also the further worsening of the general crisis of capitalism.

Bourgeois economics has a big part to play in mustering these considerable reserves, for it seeks to spin out new conceptions of state-monopoly regulation of the economy, to find more efficient methods of exploiting the working people, and to improve the methods of social manoeuvring in the midst of the sharpening antagonistic relationships between labour and capital.

However, the condition of bourgeois economics, as a component of the ideological superstructure, cannot be directly determined only on the strength of the state of the economic basis of capitalist society and the cyclical factors behind the reproduction of social capital. Its condition, like those of the other elements of the ideological superstructure, is determined by the whole of earlier history which shapes men's world outlook and their economic, philosophical, juridical, and political notions and views. That is why an analysis of the problem before us requires a circumstantial retrospect of the ideological contest between the bourgeoisie and the proletariat in the past.

What needs to be taken into account is that the crisis of bourgeois political economy broke out roughly half a century before the general crisis of capitalism. It was dealt a mortal blow by the publication of *Capital*, whose subtitle—*A Critique of Political Economy*—showed very well the importance Marx attached to the exposure of the theoretical propositions designed to justify the proletariat's exploitation. Marx's theory converted socialism into a science, into a guide to revolutionary action, which inaugurated mankind's historical transition from capitalism to socialism.

In order to specify our view of the stages in the development of the crisis of bourgeois political economy, we need to answer some of the questions arising in the discussion of this subject. Some ask: why do we claim that Marx's *Capital* dealt a mortal blow to bourgeois political economy, which has continued to exist and develop? We answer: the Great October Socialist Revolution, which took place as a result of the conversion of Marxist-Leninist ideas into a mighty material force, signalled the birth of a new socio-economic formation and the conversion of capitalism into a moribund social system.

The fortunes of capitalism are being decided

These charges are absurd.

First, Marxists never deny the bourgeois economists' priority in noting some new real processes in the economy of capitalism and in bringing out various aspects of its reality.

Second, the Marxist assumption is that genuine innovation in science does not at all consist in refuting earlier theories. True innovation is always based on advances in science borne out by practice. Our strategy in the struggle against bourgeois concepts consists in a creative development of the Marxist-Leninist political economy, which, being an open-ended system free from dogmatism, allows the inclusion within its orbit of the analysis of new uniformities of economic development.

In line with Marxist-Leninist traditions, we have never rejected the elements of scientific observation contained in bourgeois concepts, or denied the practical importance of these concepts for the economic policy of state-monopoly capitalism, which attempts to overcome some of the most outrageous contradictions of capitalist reproduction.

Ever since socialism became a reality, the crisis processes in bourgeois economics have been most closely linked with the development of the general crisis of capitalism. The "etatisation" of the economy, the ever closer coalescence of the state and the monopolies as monopoly capitalism grows into a state-monopoly capitalism, is the dominant trend in the adaptation of the relations of production to the requirements of the development of the productive forces in so far as this is possible with private property in the means of production. Bourgeois political economy has the primary role to play in restructuring the capitalist relations of production.

1. Crisis of Traditional Doctrines

With the triumph of the October Revolution, which ushered in the epoch of the general crisis of capitalism, the struggle carried on by bourgeois political economy against the Marxist economic theory moved beyond the framework of an "academic" confrontation of ideas. It now concentrated its attacks not on *Capital*, but on existing socialism, which was being built on the basis of the Marxist-Leninist theory, in a country ruined by an imperialist and a civil war, encircled by hostile capitalist countries seeking to strangle the fledgling Soviet state in the noose of an economic blockade.

The 1920s saw a temporary and relative stabilisation of capitalism. In that period, the main argument against the Marxist-Leninist economic theory and its conclusions concerning the general crisis of capitalism took the form of boasts about US economic "prosperity", and claims that the mass production and availability to some working people of relatively cheap cars and other consumer durables showed that the capitalist system was viable, sound and enduring. The ideals of socialism were countered with the first prototype of the "mass consumption society". Bourgeois economists were jubilant over the fact that "Ford beat Marx", allegedly proving the possibility of a "class peace" and the superiority of the market competition system over the Soviet ideas of economic planning. The disastrous economic crisis of 1929-33, which hit all the countries of the capitalist world, on the one hand, and the successful fulfilment of the USSR's first five-year economic development plan, on the other, made nonsense of the advocacy of the ungovernable market economy, and marked the demise of the bourgeois neoclassical school, the theoretical basis of such advocacy for many years. It was necessary to restructure bourgeois political economy, and this led to the "Keynesian revolution", when a theoretical back-up was presented for the need for state regulation of the economy as the only way of enabling capitalism to keep its ground in the contest with socialism.

Keynes's model provided for the stimulation of aggregate effective demand through government financing of public works, inducement of private capital investment, and an insignificant redistribution of the national income through the budget in favour of the have-nots. The main instruments of regulation were to be the state budget, deficit financing of the economy and manipulation of interest rates.

Keynesianism produced diverse variants of economic policy of state-monopoly capitalism. Having elaborated the instruments for regulating the economy for the benefit of the monopolies, it became increasingly important for them, as the objective prerequisites matured for the further growth of monopoly capitalism into state-monopoly capitalism determined by the concentration and centralisation of capital, the militarisation of the economy, and the logic of the development of the productive forces under the scientific and technical revolution. At the same time, Keynesianism became a necessary element of the policy of state-monopoly capitalism in view of the sharpening class struggle in the individual countries and on an international scale.

What is the reason for the rise and fall of the Keynesian cult? The answer will shed light on the current stage in the crisis of bourgeois economics.

John Maynard Keynes transformed bourgeois economics and was a founder of the bourgeois theory of state-monopoly capitalism. Although he did not go beyond the bounds of vulgar non-Marxist political economy, he turned out to be one of the most far-sighted bourgeois economists of the epoch of the general crisis of capitalism.

Let us recall that after the October Revolution, bourgeois economists stubbornly argued that the planned economy was impossible in principle and predicted its failure. Their assumption was that the only viable economic system was one in which the "invisible hand" produced a stable equilibrium as it governed the free play of competition on the market. They held that the imaginary curves of aggregate supply and demand intersected on the market, so ensuring a state of economic equilibrium. Bourgeois economists saw their task in teaching the capitalists to make efficient use of the resources at their disposal in the light of the shaping market outlook and denied the need for any government interference in the process of reproduction, believing that economic crises were an element of its self-regulation.

By contrast, Keynes was among the first to produce the most realistic evaluation of the new situation in the world created for capitalism by the 1929-33 economic crisis. He had a key role to play not only in revamping vulgar bourgeois economics, but also in making it swing towards the economic policy of state-monopoly capitalism. Here, subjective factors were also of some significance. Keynes was not only a well-known scientist who headed the chair of economics at King's College, Cambridge, but also a prominent political leader of the British Empire, with the reputation of a man who could go against the tide whenever this was made imperative by the vital class interests of the bourgeoisie. He displayed these qualities as early as 1919, when in protest against the Versailles Treaty he resigned as adviser to the British delegation at the Paris Peace Conference, and wrote a book exposing the defective strategy on which the treaty was based. At the time, Lenin made the following comment:

> "Keynes has reached the conclusion that after the Peace of Versailles, Europe and the whole world are heading for bankruptcy.

He has resigned, and thrown his book in the government's face with the words: 'What you are doing is madness'."[1]

In 1925, Keynes came to the Soviet Union to study the activity of our planning bodies. Subsequently, it occurred to him that the principles of planning had to be applied under capitalism. In November 1929, when the US Stock Market crash announced the beginning of the world economic crisis, Keynes became a member of a British governmental Committee on Finance and Industry. He had enough authority to draw attention to his efforts to renew bourgeois political economy, the need for which was convincingly argued in the dark period for capitalism in the 1930s not only by academic circles, but also by the governments of the capitalist countries. There is good reason, therefore, why his 1936 book, *The General Theory of Employment, Interest and Money*, summing up his views and the ideas that were already in the air, became a guide to action for state-monopoly capitalism, whose development was accelerated by the economic crisis of the 1930s and the subsequent depression.

Keynes's doctrine was most fully applied and tested in the United States, the country which since the 1930s has been the epicentre of all the economic crises rocking the capitalist system. Measures for overcoming crisis situations were first taken by President Franklin D. Roosevelt, whose anti-crisis measures slowed down the recession in 1937, which broke out as tempestuously as it had done in 1929.

Keynesian theory also largely influenced the economic views of the monopoly bourgeoisie during the Second World War, which sharply accelerated the development of state-monopoly capitalism.

[1] V. I. Lenin, *Collected Works*, Vol. 31, Progress Publishers, Moscow, 1966, p. 219.

For a good reason, that theory determined the principles of economic policy for the postwar period, which were being worked out towards the end of the war by the governments of the capitalist countries of the anti-Hitler coalition. The anti-fascist nature of the war and the crushing defeat of the most reactionary forces of imperialist aggression forced the capitalist governments of the anti-Hitler coalition countries to promise their peoples that after the war they would ensure "full employment" and set up a system of social security ensuring the working people against poverty and hunger in the event of any future crises.

Keynesianism helped to substantiate the economic policy of bourgeois reformism effected with the preservation and further development of state-monopoly capitalism.

In the postwar period, Keynesianism became the leading theory of bourgeois economics providing the basic principles for the economic policy of the capitalist countries.

In the United States, where powerful monopolies had the most modernised production facilities, the Keynesian policy of state-monopoly regulation was oriented upon the development of the military-industrial complex with the use of the latest advances in the scientific and technical revolution rather than upon structural changes in the whole of the economy. Of much importance in substantiating this economic policy was the myth circulated by the advocates of militarism concerning the beneficial effect of military expenditures on the living standards of every section of the US population.

The role of Keynesian methods of economic regulation grew markedly in the 1950s and 1960s. Keynes's old model, which provided mainly for measures to avert periodic crises, gave way to neo-Keynesian "dynamic models" which claimed to provide a policy for sustained growth. Alongside the short-term policy of evening out the phases of the cycle, attempts were made to implement a purposeful state policy for medium-term and long-term programming and planning of the economy. This not only stimulated the growth of the economic strength of the monopolies, but simultaneously modified the sectoral structure of the economy in the light of the trends in the scientific and technical revolution for the purpose of enhancing the country's competitiveness on external markets. Such a policy was most conspicuously pursued by West European countries and Japan.

There were many reasons for the increase in economic growth rates in the developed capitalist countries, among them, most importantly, the successes scored by the working people in securing higher living standards through the class struggle, a fact which helped to expand markets through increased manufacture of consumer durables. But, ignoring the deep-seated contradictions of capitalist reproduction, determined by the development of its general crisis, bourgeois economists ascribed this to the effectiveness of the "growth policy" and extolled it as being capable of stabilising capitalism.

The positions of Keynesianism were also fortified by the fact that from the second half of the 1940s to the mid-1960s there were no economic crises of appreciable depth in West European countries practising the Keynesian principles of regulation. The almost eight-year-long economic boom in the United States in the 1960s, unparalleled in the postwar period, was proclaimed by the Keynesians to be a triumph of Keynesian economic policy.

But as early as the mid-1960s, even superficial observers of the market situation increasingly realised that the Keynesian policy of stabilisation and growth effected by methods of deficit financing posed the threat of transforming "regulated", "creeping" inflation into snowballing inflation.

In the early 1970s, the "regulated inflation" recommended by Keynes, which had been regarded as an expression of supreme wisdom in the economic policy of state-monopoly capitalism, developed into "galloping" inflation. When Keynes was working on his theory, mass unemployment was regarded as the main social danger facing capitalism. Since the early 1970s, however, the governments of developed capitalist countries have been forced to declare inflation Enemy No. 1, for it had first reached catastrophic proportions in peacetime.

The mounting inflation, engendered by the state's growing involvement in regulating the economy, and the economic upswing itself led to a gradual revival of neoclassical theory in the 1960s. Neoclassics put forward their own economic growth models, which made them serious rivals and critics of Keynesianism. This was promoted by the support they got from that part of the monopoly bourgeoisie which objected to excessive state intervention in the economy. The political credo of this trend—that the role of the state should be confined to the sphere of credit and monetary regulation, and that the rights of the trade unions in their struggle for higher wages should be tightly policed—met the interests of the most reactionary forces of monopoly capital.

Theoretically refurbished, the neoclassical trend began to take over the traditional spheres of Keynesianism: the theory of economic growth, analysis of economic instability and the cycle, monetary and financial relations, etc. The coexistence and contest of the two trends in non-Marxist political economy produced an urge to merge them in a more general conception in line with the traditions of the give-and-take bipartisan policy actually practised by the legislature and the executive in the United States, in spite of all the loud electoral debates between the two bourgeois parties.

This produced the "neoclassical synthesis" concept, which is designed more broadly to back up state-monopoly capitalism as a system, combining the ungoverned mechanism of the market with indirect measures of government regulation. "Neoclassical synthesis" became the theoretical substantiation for a "mixed economy".

However, "neoclassical synthesis", the supreme achievement of bourgeois economic thought of the late 1960s, designed to fuse the ideas of the neoclassics and the neo-Keynesians and to do away with their differences, proved to be a very flimsy structure indeed. It began to fall apart under the blows of the sharp aggravation of the social and economic contradictions of capitalism in the late 1960s and early 1970s, and this led to acute flare-ups of polemics between the neo-Keynesians and the neoclassics both on theoretical issues and on the practical approaches to state-monopoly regulation of the economy.

The socio-political crises which broke out in some countries with a relatively favourable market outlook caught the bourgeois economists completely unawares. This chain of events includes the powerful 1968 strike movement in France and the subsequent resignation of the de Gaulle government, which its consequences induced; the similar working people's movement in Italy in 1969, which strengthened the positions of the left forces; and the unrest in the black ghettos, and the mass movement in the United States against the war in Vietnam, which forced President Johnson to withdraw from the presidential race in the 1968 elections.

Equally unexpected for the bourgeois theorists were the qualitative changes in the process of reproduction, which destroyed, one after another, the postulates on which their concepts were based. Among these changes was, above all, the rapid development of inflation not only in the up-phase but also in the crisis years.

The pathological changes in the US economic organism and its inability to cope with the inflation were revealed during the 1969-71 economic crisis, which broke out during the US war in Vietnam. That was the first crisis in the history of the United States in which prices continued to grow.

The deep disruption of the reproduction mechanism was also revealed in the economic upswing which began in 1972-3, and which developed into a feverish inflationary boom. In view of the leapfrogging growth of prices, the big corporations built up their stocks through excessive inventories of fuel, raw materials, and other goods. This produced acute shortages of many goods, sharpening the energy and raw material crises and further pushing up the price spiral. The inflation spread ruin among the medium and small firms which did not have the money to build up stocks of fuel and raw materials because of rising prices and could not obtain credits because of the sharp rise in the interest rate. In this way, the inflation which accompanied the boom dampened it down.

In 1974, the capitalist countries entered into a world economic crisis with continued inflation and growing unemployment.

The crises of 1969-71 and 1974-75 revealed that the "Phillips curve", which bourgeois economics had accepted as an axiom, and which suggested that growing unemployment was the best antidote for inflation, had become invalid. It turned out that, in spite of the "Phillips curve", there was a simultaneous growth both of inflation and unemployment in some countries.

It became perfectly evident that the Keynesian doctrine of state-monopoly regulation of the economy, designed to stimulate it by means of budget deficits and militarisation, had failed. The flexible manipulation of interest rates proved to be impossible because these had to be pushed up, making credit more expensive. Under "galloping" inflation. the lender seeks to have the borrower pay for the risk he incurs in view of the depreciation of money, The difficulties of using Keynesian instruments to check the growing anarchy in the capitalist economy have been compounded by the collapse of the Bretton Woods international payments system based on Keynes's conception. The crisis of the dollar, as expressed in its devaluation and the end of its convertibility into gold in 1971, made it extremely difficult to apply Keynesian methods in regulating not only foreign-exchange relations but also monetary circulation within individual countries. The flood of dollars not based on gold and moved from one country to another by multinational corporations for speculative profits made the inflationary process even less controllable.

These new phenomena not only discredited the dogmas of Keynesianism, but also tripped up the neoclassics by depriving them of their most important argument against the Keynesian policy of "full employment", which they regarded as the main cause of inflation. The neoclassics, led by the US economist Milton Friedman, the most aggressive opponent of Keynesian theory, held that the surest way of getting rid of inflation was to return to the "normal" cycle with mass unemployment in time of crisis. But because of the unusual course of the crisis, they themselves had to concede that the growth of unemployment tended to produce social consequences that were as dangerous as those engendered by the inflationary process, and to recognise the need for deficit financing to combat unemployment.

The dollar crisis also brought out another circumstance which compromised the neoclassical doctrine: it turned out that so-called administration-dominated prices had risen to the highest level. It was becoming obvious that it was not only the state with its policy of deficit financing that was to blame for the inflationary process, but also the big corporations, whose market policy the neoclassics had held up for orientation.

Meanwhile, the Marxists have long been aware that the inflationary process is fuelled by the system of state-monopoly capitalism. It is noteworthy that this conclusion has been unwillingly accepted by some bourgeois economists.[1]

Thus, in the late 1960s and early 1970s, the neo-Keynesian and the neoclassical theory, together with the theory of "neoclassical synthesis" as a whole faced a profound crisis. They had demonstrably failed to cope with the aggravated socio-economic contradictions of capitalism. Having proved incapable of proposing any effective means for easing the economic situation which had taken shape in the leading capitalist countries, the partisans of the two schools blamed each other for the failures of economic policy.

Bourgeois political economy was confronted with the need for yet another review of its obsolete dogmas and a search for new concepts.

2. "Reappraisal of Values"

For all the substantial distinctions between the crisis processes in non-Marxist political economy in the 1930s and the 1970s, their development has one outward similarity: on both occasions, these came for bourgeois economists like a bolt from the blue. On both occasions, they had been lulled by the semblance of prosperity produced by the economic outlook, which they claimed to be evidence of the correctness of their concepts. On the eve of the 1930s, this deceptive state was produced by "prosperity" in the United States, and in the 1950s and 1960s, by the unprecedented rates of economic growth in the industrialised capitalist countries.

The contradictions between the traditional schools

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[1] See: G. Means, "The Administered Price Thesis Reconfirmed". In: *The American Economic Review*, June 1972, Vol. LXII, No. 3, p. 292.

of bourgeois political economy—the neo-Keynesians and the neoclassics—have always been pivoted on the issue of the limits and forms of government intervention in the economy. The Keynesians emphasised budget instruments, while the neoclassics gave priority to credit and monetary methods, with government enterprise cut down to a minimum.

At the present stage in the crisis of bourgeois political economy, this issue has become less relevant and has given way to another burning problem: which methods are to be used in state-monopoly regulation?

The inability of bourgeois political economy to provide the ruling elite with reliable guidelines for economic policy inevitably led to bitter disappointment in that which had only the day before been the object of their veneration. Most Western economists recognised the need for a critical review of the traditional approach to economic analysis.

The "orthodox" political economy (as represented by its two branches, the Keynesian and the neoclassical) is now being sharply criticised by the socio-institutional trend with its much broader approach to the analysis of socio-economic problems. In the early 1970s, the US economist John K. Galbraith, the most prominent spokesman for this trend, became the most popular economist.

The growing role of the socio-institutional trend is a reflection of the urgent need for the ruling class to find a new approach to the state-monopoly regulation of the economy. This is due to the achievements of socialism and the working-class movement, and the need to reckon with the much higher level of the working people's socio-economic demands, which are embodied in a system of values determined by the concept of "quality of life" and reflect the growth, under the impact of the scientific and technical revolution, of the role of the social and moral factors in the value of labour power, and the transformation of the working class into society's chief social force, which is increasingly aware of its historic importance.

There has also been a growth in the influence of the radical wing of bourgeois political economy, some of whose spokesmen want to renew it by borrowing certain Marxist propositions. Along with this peculiar brand of "legal Marxism", traditional vulgar political economy is also being crowded by the "new left", claiming to represent a "renewed Marxism".

However, a sizable majority of bourgeois economists not inclined to give up the traditional ideas and concepts believe that the problem can be solved through a further synthesis of various trends in bourgeois economics. Among those who advocate this is Paul A. Samuelson, who has already tried to effect a "synthesis" of the neo-Keynesian and neoclassical trends.

Samuelson said it was wrong to take a one-sided approach to the problem of growth only with a view to increasing the GNP, outside the context of the problem of its distribution. He reached the conclusion that it is better to have a smaller "national cake" but more fairly distributed among the population, than to look to the prospect of its growth without taking into account the attendant social costs. Samuelson asserted that reforms were required to achieve optimal conditions for the growth and distribution of the GNP, but that there should be no amateurish solution of the problems of reforms. It is up to economics to formulate the new concepts to back up and put through these reforms.

> "In short, economic analysis is the indispensable handmaiden of those who seek social reforms and of those who wish to preserve and conserve the inherited order."[1]

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[1] P. A. Samuelson, *Economics*, McGraw-Hill, 8-th ed., New York, 1970, p. 763.

The purpose of such reforms is obviously to "preserve and conserve" capitalism. Economists, Samuelson believes, should concentrate on research into reforms without social upheavals.

In asserting that the problem of a fair distribution of the "national cake" can be solved without a social revolution, Samuelson brushes off the impoverishment of the proletariat, a uniformity established by Marx. He distorts history in an effort to prove that capitalism has an inherent tendency to move towards abundance. He regards capitalism as a closed system with an inherent capacity for the most effective increase of wealth, and ignores the incontrovertible fact that the "welfare state" which he extols, and which he believes can operate on the basis of bourgeois reforms, could not exist even as a theoretical model if capitalism had not been forced to retreat under pressure from the world revolutionary forces. In defiance of the actual historical facts, Samuelson presents the "welfare state" as a spontaneous product of capitalism itself. We are told that it was unaugurated by Gladstone and Disraeli in England, Bismarck in Germany and Franklin Roosevelt in the United States. Since then, as a result of the redistribution of taxes and the development of public education, there has allegedly been a steady reduction of the inequality among people, with capitalism moving towards ever greater justice.[1]

Samuelson, it is true, admits that great fortunes and inherited wealth still make for the greatest disparities in income, but he holds that revolutionary methods should not be used to do away with this injustice through a confiscation of large-scale property, because justice and efficiency in production are incompatible. The confiscation of property, he believes, might slow the growth of production and create barriers to the movement of capital

[1] P. A. Samuelson, *op. cit.*, p. 764.

into the most efficient industries. He believes that the way out lies in a combination of state and private enterprise, i.e. in a "mixed economy", which could allegedly provide the only basis for a "welfare state".

> "Through *direct* public services and through *transfer*-payment programs, the modern mixed economy is in effect a gigantic *system* of *mutual insurance* against the worst economic disasters of life."[1]

But Samuelson's vision of a social harmony allegedly created by the "welfare state" cannot ensure a "class peace", even in the United States. He is forced to admit that there was no delight or gratitude among deprived Americans over the social welfare programme designed by President Nixon to have the government provide every family with a minimum guaranteed income.

Having reached the conclusion that "many more people favor guaranteed jobs than guaranteed *incomes*", he makes a highly significant admission, which is so important for characterising contemporary capitalism in a country like the United States, the citadel of free enterprise, where government intervention in the economy was not long ago regarded as "creeping socialism".

"Some people have proposed," Samuelson writes, "that the *government be the employer of last resort*: anyone who cannot get a decent job from private industry should have the right to a job from the government."

He goes on to draw the following conclusion:

> "If a program to guarantee jobs were as feasible as a program to guarantee minimum incomes, work for all would surely be a preferable alternative."[2]

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[1] *Ibid.*, p. 771.
[2] *Ibid.*, p. 775.

Samuelson admits that the United States government, for all its increased strength, is dependent on influential economic forces, above all those linked with the military-industrial complex, forces which want to prevent broad government intervention in the employment problem, and are not inclined to make concessions to the working people. He is aware of the need for such concessions in present-day conditions, and says that there is no reason "for permitting a military-industrial complex to be the arbiter of our national policy".[1]

Samuelson seeks to convince the businessmen among his readers, for whom his *Economics* has become a bedside book, that they have to take into account the need for social manoeuvring and the inevitability of growing government intervention in economic life, which is bound to embrace more and more spheres. He points, in particular, to the government's exceptional role in tackling the new economic and social problem of environmental protection.

There is good reason why Samuelson is worried about the ecological problem. In the United States, more so than in any other country, those "who make profits" do so mostly not only through the use of higher technology and subtle forms of labour power exploitation, but also largely through plunderous destruction of the environment, something the capitalists were until recently given a free hand to do. But the class struggle is increasingly becoming a barrier to business initiatives along these lines.

Even in the 19th century, resistance by the working class forced the bourgeois state to put curbs on the capitalists' most frenzied drives for profit and to legislate on the length of the working day, on safety and other measures ensuring the necessary conditions for protecting the working people's life

[1] P. A. Samuelson, *op. cit.*, p. 778.

and health. Today, the working people's struggle for these same goals and the demands for environmental protection have been further intensified. The uprisings in the social ghettos of the big cities in the United States, where people are downtrodden not only by the oppression of poverty but are also literally doomed to asphyxiation because of the lack of clean air, have forced the ruling elite to think about legislation limiting the power of the owners of capital over the environment and the right they have arrogated to destroy it.

Samuelson notes that this must inevitably intensify government intervention in the economy:

> "These 'economic externalities and diseconomies' cannot be expected to be set aright by market competition and the pursuit of profit. They call for government zoning ordinances, fiats and prohibitions, planning and coordination, subsidies and penalties of taxation."[1]

One should bear in mind that this entails more than the use of the government's administrative power. Environmental protection requires government programmes for remodelling old plants and building new ones, rebuilding the highway network, relocating industry, installing new technical facilities in the energy and fuel industries, developing and stimulating the manufacture of devices for purifying air and water, destroying and recycling waste, etc. The scope of state-monopoly business is markedly enlarged by government intervention in environmental protection, which is determined by the sharpening class struggle and the emergence of its new forms, and also by the need to ensure overall conditions for the expanded reproduction of capital.

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[1] *Ibid.*, p. 794.

One would think that a new sphere of business holding promise of profitable investment must give bourgeois economists a sense of optimism. But that is far from being so. They realise that the growth of the public sector in ecology-related industries accelerates the US advance to a so-called mixed economy with all its inherent contradictions, which tend to undermine the autocratic power of private monopoly business and make for socio-economic instability.

So, in the late 1960s and early 1970s, Samuelson was forced considerably to amend his theory of "neoclassical synthesis", producing a version which, we find, now contains, on the one hand, the Keynesian and the neoclassical trends in bourgeois political economy insisting that the crux of economic policy should be government influence on the haphazard market processes, and on the other, the socio-institutional trend which brings to the fore non-market regulation of the economy on the basis of long-term agreements between the government, the big corporations, and the trade unions.

Trends towards a theoretical rationale of the new recommendations for state-monopoly regulation are in evidence not only on the macroeconomic level but also in microeconomics, within the framework of individual companies, where more flexible systems of industrial management reckoning with the social factors of its organisation are mooted alongside the traditional managerial methods based on tough authoritarian principles of Taylorism and Fordism.

A significant symptom of these changes since the Second World War has been the introduction of the postulate of "human relations" into the system of capitalist rationalisation of industrial management.

This socio-technical system of management was taken a step further with the efforts on the part of capital to exert an influence on "minor groups" of workers at the enterprise, an approach which seeks to take into account not only the physical but also the moral and mental potentialities of every worker.

In short, instead of the "machine—man" system, which emerged with the development of the conveyer-belt system and on which Taylorism and Fordism are both based, the socio-technical concepts of capitalist rationalisation increasingly entail efforts to improve the "man—machine" system.

The socio-technical approach to management is based on the idea of applying capitalist rationalisation not only to the technological system of the enterprise but also to its social structure. It is based on the assumption that employers and workers can reach "productivity agreements" and so leave the impression that the master—servant system in industry has disappeared. The purpose of this socio-institutional approach to management is to create the illusion of self-management at the capitalist enterprise based on the principle of "social partnership".

These trends in the evolution of management show that the scientific and technical revolution has been preparing the material prerequisites for socialism not only on the scale of the capitalist society as a whole, but also within the framework of individual enterprises, where efficiency cannot be raised without an imitation of some of the elements of ostensibly new relations of production. The "minor group", set up at the capitalist enterprise to make use of the advantages of collective labour, tends, in effect, and despite the wishes of the capitalists, objectively to negate the traditional "master and servant" principle and the barrack-room atmosphere in which orders are issued and fulfilled, the basis of the capitalist relations of production, so creating the social prerequisites for their abolition.

The practice of the class struggle in many developed capitalist countries of Western Europe has repeatedly demonstrated the ability of modern well-educated and skilled workers to manage production not only within "minor groups", but also on the scale of the whole enterprise, by rallying the managerial, engineering, and technical staff to take over the running of the whole business. It is this terrible prospect of the economic struggle of the working class growing into a political struggle that has forced bourgeois political economy to revise its ideas in the light of the new objective conditions which have taken shape at the present stage of the general crisis of capitalism.

It is the realities of the class struggle rather than the naggings of an awakening conscience that impel the capitalists to realise the need for some "humanisation" of the forms in which labour is exploited. There is good reason why a law on the "humanisation of labour" was passed in France after the historic massive strike of 1968. Another characteristic fact is that under the pressure of new demands in the working-class movement a special ILO report to the 1974 European Conference recommended the application of socio-technical and ergonometric principles of industrial organisation and the formation of new autonomous teams to provide more opportunities for worker participation in management.

3. Renewal of the "Mixed Economy" Theory

The class solidarity of bourgeois economists in the search for ways to fortify the capitalist system has been growing with the mounting economic, social, and political instability in the developed capitalist countries, where there is growing awareness among the working people of the need to join forces for dealing a blow at the whole system of state-monopoly capitalism.

Whatever the stand taken by the various bourgeois economists, they have one common purpose, which is to refurbish the "mixed economy" theory and to find new methods for state-monopoly regulation of the economy.

Many Western economists, including Samuelson, believe that Galbraith's proposal for price control is a new way of tackling the problem. What is wrong with the theory and policy oriented upon the market outlook, according to Galbraith, is that these ignore the decisive role of large corporations in price formation.[1]

Galbraith insists that the market is on the way out and asserts that prices are, for all practical purposes, fixed by the big corporations and the trade unions, which is why the government now no longer needs a big bureaucratic apparatus to control prices, because this relates only to the big organisations. Wage and price control requires hard bargaining between the unions and the corporations. The unions will agree to a wage ceiling only when they are sure that there will be no inflation. That is why it is necessary to work out definite guidelines for the growth of wages and to apply the laws when these are breached. Galbraith believes that government price control should not be temporary but permanent, and assumes that the government will have to bargain with several hundred trade unions and several thousand corporations to lay down average price ceilings. Direct administrative control of wages and prices will make it possible to lower interest on credit. This will stimulate small enterprises and increase employment without further inflation, because the prices of most enterprises outside the corporate system are subject to the law of free market competition which prevents the growth of inflation.

Galbraith's call for administrative government

[1] See: *L'Expansion*, February 1971.

influence on the big corporations with respect to prices marked a review of his own theory of "mature corporations", which allegedly have a stake in expanding demand by lowering prices.

Slower growth is another way suggested by bourgeois economists for solving the acute problems of the contemporary "mixed economy".

Galbraith believes that the way out of the contradictions of the "affluent society" lies not only in tough price controls but also in the abandonment of high growth rates, a reduction of excessive consumption and a consequent improvement of the "quality of life". He looks both to reforms and to subjective psychological factors, because

> "in the United States, and to a lesser extent in Britain and Europe, a whole generation is rejecting the standards of persuaded and competitive consumption.... Once people discover that they are enslaved by their consumption ... they seek emancipation, and for good."[1]

Characteristically, Galbraith does not deny the crucial role of the working class in seeking a way out of the social conflicts of the "consumer society", but oddly enough says that the working class is to blame for the "excessive" consumption. He declares:

> "In both the United States and Britain most trade unionists still want to increase their consumption—I think with reason. The idea of a new life style is getting its foothold first in the middle class..."[2]

So, there is a growing understanding among bourgeois economists and big business of the need for bourgeois reformist manoeuvring on the basis of close interaction between government and mo-

[1] *The Observer*, November 22, 1970, p. 25.
[2] *Ibid.*

nopolies. Thus, Jay McCulley said in an article entitled "Big Business and Revolution" that in the United States, for instance, social matters were of increasing concern to employers who had earlier believed that these were none of their business. The same evidence comes from articles in the business press urging the need for tax measures to bring about a "revolution" in the distribution of profits between shareholders and working people, between businessmen and society. Some regard such reforms as signifying the end of capitalism, continues McCulley. He urges everyone to make concessions in the spirit of this dictum of Henry Ford's: "Let us not argue about terminology: we must either adapt or die."[1]

The same ideas were expressed by the US economist Neil H. Jacoby, whose book[2] was published with the blessings of Arthur Burns, one of the pillars of the neoclassical school in the United States. Jacoby calls on the government to do everything towards using the positive importance of the corporations in keeping free competition "viable" while encouraging the growth of their role in solving social problems. He tries to prove that the self-seeking drive for profit is quite compatible with an awareness of social responsibility by corporate business, especially if this is induced by government regulation and fiscal policy. He believes that the corporations could play a key role in attaining the "national goals" of the United States if business is judged not only as an economic agency but also as a "political" agency governing the working lives of its employees.[3]

We find, therefore, that even the spokesmen of the most conservative bourgeois economic thinking

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[1] *Le Monde*, July 27, 1971, p. 11.

[2] N. Jacoby, *Corporate Power and Social Responsibility*, Macmillan Publishing Co., New York, 1973, p. 13.

[3] *Ibid.*, p. 16.

are inclined to accept some compromise version of a "mixed economy".

It would be wrong, however, to underestimate the contradictions between the conservative and the liberal camps in bourgeois economics, which stand out in formulating specific programmes for economic policy and which have an important role to play in the struggle for power among the bourgeois political parties.

The "mixed economy" in the spirit of the theoretical concepts of Samuelson and Galbraith provides for active government intervention in the economy through extensive use of the "incomes policy" mechanism. They propose that this policy should be made a permanent one so as to ensure more rigid control of prices and wages in a flexible combination of administrative measures and economic stimulation. Samuelson and Galbraith assume that the US Administration can reach agreement on the terms for such control with several hundred big corporations as the latter come to realise the impending social danger and their best interests, and have to accept such an "incomes policy" for the sake of the "national" interest.

In addition, Samuelson and Galbraith hope that the government's positions will be strengthened through an extension of its entrepreneurial activity within the framework of the "mixed economy". They believe that the government's economic functions will be further extended in view of the necessary growth of its role in building up the infrastructure, its ever greater involvement in effecting and financing research and development projects, and measures to improve the environment. They attach much importance to a redistribution of the national income by the government through a reduction of the military budget and an increase in the share of transfer payments to implement social programmes.

The neoclassics are highly alarmed over the government's growing role in the "mixed economy", for they look to the broadest possible initiatives on the part of big business in using the advantages of market competition. But it goes without saying that Samuelson and Galbraith's proposal for much broader economic functions for the state in the "mixed economy" is not at all aimed to weaken the positions of big business. Their objective political purpose is to tighten up the system of state-monopoly control and to weaken the strike movement of the workers, whose struggle for higher wages is allegedly chiefly to blame for the fact that society has to suffer from inflation, from the costs engendered by stepped-up economic growth, and the consequent destruction of the environment.

In Western Europe, where socialist ideas have much deeper roots in the working-class movement, which in some countries has a strong communist vanguard closely bonded with other left forces by traditions of joint struggle against fascism, bourgeois reformists cannot base their theoretical studies on the assumption that the traditional institutions of state-monopoly capitalism are immune.

In France, for instance, most bourgeois economists advocate ideas of structuralism, which are characteristic of the sociological trend in political economy. Their proposals for structural improvement do not rule out nationalisation, but even there the main effort is to find structures in which the state could most effectively make the working people submit to the terms of "class peace" on the basis of an "incomes policy".

We shall subsequently see that well-known bourgeois economists seeking new "mixed economy" concepts do not go beyond a rehashing and modernisation of their own earlier doctrines.

4. Western Economists' View of the Crisis and New Attacks on Marxism

A peculiar feature of the present crisis of bourgeois economics is that for the first time in its history an overwhelming majority of bourgeois economists admit the fact of the crisis. But there are sharp differences among the various schools over the nature of the crisis. Because their political economy is apologetic, these differences largely resemble a "family quarrel" and consist mainly in apportioning among the various schools the blame for the failures in the economic policy of state-monopoly capitalism. There is talk of miscalculations in analysing the situation, structural changes in the economy, and budget or monetary policy. Understandably, no bourgeois economist has considered the built-in antagonistic contradictions of capitalism itself.

Economists outside the traditional schools of bourgeois economics took the initiative in criticising the bankrupt theories. They mounted a general offensive at the annual meeting of the American Economic Association in December 1971, when its President was Galbraith, who invited Joan Robinson, the well-known British economist, to give a report analysing the present crisis of bourgeois political economy.[1] She said that economic theory was now going through its second crisis, the first having led to the emergence of Keynesianism. But her interpretation of the substance of the crisis was one-sided

First, she considered the crisis of bourgeois economics outside the context of the objective uniformities of the general crisis of capitalism, and completely ignored the impact of Marxist-Leninist political economy on the processes going on within it.

[1] See: J. Robinson, "The Second Crisis of Economic Theory". In: *The American Economic Review*, May 1972, Vol. LXII, No. 2, pp. 1-10.

Second, she argued that the main concern of the critics of the traditional schools of bourgeois economics was to elaborate a new theory to explain contemporary reality allegedly for the purpose of enhancing the peoples' well-being.

Third, her "second crisis" theory suggested that the crisis had originated from the defects of the neoclassical school, which Keynes had criticised in his lifetime but not to the full extent. Robinson, speaking for the Keynesian left wing, held that the crisis could have been avoided had Keynes, in his efforts to fortify capitalism, not ignored the question of solving social problems with an eye to the trade union demands on wages and working conditions. She backed the socio-institutional trend and criticised the Keynesians for having ignored important factors like the development of education, public health, and protection of the environment.

Consequently, it was all a matter of failures in theory, without a word being said about the deep-rooted uniformities of state-monopoly capitalism itself.

However, developments have shown that all the recommendations of bourgeois economists aimed to overcome the cyclical crisis besetting the capitalist world (including those of the critics of the neoclassics and neo-Keynesians) continue to lie largely within the framework of the traditional methods of capitalist anti-crisis regulation. This also explains why, for instance, Walter W. Heller, onetime head of the Council of Economic Advisers under the US President and President of the American Economic Association, delivered a report at its annual meeting in December 1974 in an effort to rehabilitate Keynes and give a different reading to the crisis of bourgeois economics.[1]

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[1] See: *The American Economic Review*, March 1975, Vol. LXV, No. 1, pp. 1-26.

Heller's views were echoed by John Hicks, who objected to the neoclassical, notably monetarist, interpretation of inflation and insisted that inflation was not rooted in the mechanism of the monetary sphere (i.e. in the correlation between the money mass, incomes, and the rate of interest), but in the sources fuelling the two different types of inflation: demand-pull inflation and cost-push inflation.[1]

The key problem of inflation, according to Hicks, is the behaviour of those who receive wages. Hicks rejects what he believes to be the obsolete monetarist views of the labour market, because a large part of the wages is determined on the basis of long-term contracts with trade unions. The wage level becomes a political question and depends on the trade unions engaged in a struggle to maintain their real wages without considering the situation taking shape on the labour market as a whole.[2]

Consequently, according to Hicks, the whole point is to make the trade unions accept some form of "wage freeze".

There is good reason why the apologetic interpretation of the crisis of bourgeois economics is paralleled with new attacks on Marxism, for there is a growing interest in the latter in view of the inability of non-Marxist economics to produce a genuine scientific analysis of the deepening crisis of capitalism. This does not concern the anti-communist and anti-Soviet concepts which are being broadly used as propaganda weapons by the mass media, but rather the anti-Marxist constructs of the bourgeois economists whose ideas are written into textbooks and monographs as "fundamental" ones.

A new line here is the resumption of the old search for "contradictions" between Volume One

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[1] J. Hicks, "What Is Wrong with Monetarism". In: *Lloyds Bank Review*, October 1975, No. 118, p. 1.

[2] *Ibid.*, pp. 2-3.

and Volume Three of *Capital*, which was started by Böhm-Bawerk in the 19th century, and which is still used as a method to falsify Marxism.

Thus, some bourgeois theorists assert that the problems arising from the exploitation of the working class dealt with in *Capital* are no longer relevant to present-day capitalism because conditions have allegedly been created for the growth of living standards, so that it only remains to do away with the alienation of the individual, which is allegedly equally proper to capitalism and to socialism.

Others say that Volume Three of *Capital* refutes the conclusions of Volume One concerning the proletariat's transformation into a majority of the population, and that this allegedly proves the possibility of a revival of the "middle class" as the decisive force of society. They insist that Volume Three provides theoretical arguments for capitalism's inevitable transformation into an "industrial society", so suggesting that Volume One has now become quite meaningless because it is too abstract.

All of this is designed to upset the logic of *Capital*, on which the economic substantiation of the inevitability of socialist revolution is based.

We find that the efforts to consign Volume One of *Capital* to oblivion are greatest, because it contains Marx's analysis of the categories of bourgeois political economy and subjects it to a withering critique. He also brings out the deep-rooted uniformities governing the development of capitalism and making its collapse inevitable. Volume One sets forth the substance of Marx's chief discoveries: the two-fold character of labour embodied in a commodity, the role of labour power as a commodity, and the conditions for the production of surplus value. In accordance with his method of scientific abstraction and transition from the abstract to the concrete, in Volume Three, relying on the analysis of the production of surplus value, which he carried out in Volume One, Marx examines its transformed form—profit—and the competitive struggle between various groups of capitalists for the distribution of the total fund of surplus value. Volume One analyses the economic prerequisites for the development and sharpening of the main antagonism of capitalist society (that between the bourgeoisie and the proletariat), which is ultimately resolved only through a victorious socialist revolution. Volume Three deals for the most part only with the antagonisms within the capitalist class arising from its struggle for profit. That is why it is so important for the bourgeois apologists to consign Volume One to oblivion and to present Volume Three as the most concrete description of capitalist reality, which Marx was allegedly only able to give after shedding the "superfluous abstractions".

Bourgeois economists seek to find new arguments for discrediting the Marxist political economy, for there is a growing interest in it as their own theoretical helplessness is increasingly brought out.

The search for mistakes in the theory of Marxism-Leninism does not increase the political capital of bourgeois economics but merely testifies to a deepening of its crisis. This is due not only to subjective factors or epistemological mistakes by individual schools, as bourgeois apologists claim in their efforts to refurbish and modernise their economic theories. We believe that the fundamental reason why bourgeois economics has run into a dead end, is its neglect of the objective uniformities of the general crisis of capitalism and of the inevitable transition from capitalism to socialism on a world scale.

Back in 1864, Marx wrote about

> "...the great contest between the blind rule of the supply and demand laws which form the political economy of the middle class,

and social production controlled by social foresight, which forms the political economy of the working class."[1]

Historical development dictates the objective need for social regulation of production in the developed capitalist countries, which is ever more social in character. This function cannot be performed by the capitalist state, which has been using all its potentialities to slow down the revolutionary process and stabilise capitalism while keeping its private-monopoly basis intact. It is not capable of refuting the laws of history.

The economic development of the industrialised capitalist countries has fully borne out the conclusions drawn by the 24th and 25th congresses of the CPSU, which said that all the efforts to stabilise capitalism through a preservation of monopoly power are futile. The Peace Programme, put forward by the 24th Congress and further elaborated in concrete terms by the 25th Congress, reflects the objective imperatives of world development. It indicates the effective means for ridding the nations of many of the dire consequences produced by imperialism's post-war economic and political strategy of the cold war.

It is noteworthy that many bourgeois economists have resolutely come out for detente, and for peaceful coexistence and cooperation between the two systems. This is fresh evidence of the crisis of the strategic doctrines of bourgeois political economy which used to feed the cold war ideology.

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[1] Karl Marx and Frederick Engels, *Selected Works* in three volumes, Vol. Two, Progress Publishers, Moscow, 1969, p. 16.

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Part One

CHAPTER ONE

EVOLUTION OF ECONOMIC GROWTH THEORY

Let us start our analysis of the present state of bourgeois political economy with the theory of economic growth. It has developed in the form of abstract models designed to establish the interrelationship and interdependence of the main categories of reproduction and the pace of its expansion. The growing role of the practical function of bourgeois political economy has stimulated the demand for such a theory as the basis for long-term state-monopoly regulation of the capitalist economy, and for an apologia of capitalism.

The theory of economic growth has gone through a number of stages: from Keynes's macroeconomic theory to the emergence in the mid-1950s of the Keynesian version of the theory of growth, for which the Harrod-Domar model provided the initial basis. From about the mid-1950s, the growth theory was elaborated by neoclassical economists, among them J. E. Meade and Robert Solow, who sharply criticised the Keynesian notions of the economic growth mechanism and proposed their own models which provided the basis for the development of the neoclassical version of growth theory.

Earlier on, we spoke of the reasons for the peculiar "neoclassical resurgence" in about the mid-1950s, when the neoclassics began to take over many areas of economic analysis.

Apart from the general reasons (the mildness of the economic crisis, the growing government intervention in the economy, and the mounting inflationary process), a number of particular circumstances promoted the development of neoclassical theory. The premises for the internal stability of the capitalist economy contained in the neoclassical model were more to the liking of that part of the monopoly bourgeoisie which sought to limit the sphere of government intervention in the economy. The neoclassical models of growth made it possible to return, in a somewhat renewed form, to the vulgar theory of distribution, without which the theory of growth turned out to be incomplete. Finally, they provided the basis for a broader analysis of the factors of potential economic growth. All of this explains why the 1960s were a period of predominant development of the neoclassical version of growth theory, and also of attempts to blend the neoclassical analysis of long-term growth and the Keynesian analysis of economic fluctuations in a more general "synthetic theory".

1. Evolution of Economic Growth Theory. Development Peculiarities of Neoclassical Theory

A theory of economic growth, whatever its form—Keynesian, neoclassical, or neoclassical synthesis—presents two groups of problems: the problems of the factors which determine potential long-term growth of the national income, and the problems of the conditions which ensure a "steady state" of the economy (self-sustained growth), in other words, the conditions for a dynamic equilibrium, and also the question of how the economy adapts to this "steady equilibrium".

While the analysis of the long-term growth factors has run mainly along empirical lines, the "steady state" problem has been the substance of theoretical speculations and further elaboration of abstract models of economic growth.[1]

In economic growth theory, the "steady state" (self-sustained growth) has had the following main features, which the British economist Nicholas Kaldor defined back in 1958 as a group of "stylised facts" characterising the long-term trends in the economic development of capitalism:

—stable rates of growth of labour productivity and the national income (with a constant rate of population growth);

—stable rates of capital growth, and also of the "capital-labour" ratio;

—a trend towards a constant "capital-product" ratio;

—a stable rate of profit and of the share of profit in the national income.

This group of "stylised facts" provided the basis for the hypothesis that an economy with constant rates of product, employment, and capital growth, with a stable "capital-product" ratio and stable relations of distribution is in a state of dynamic equilibrium. Theory had to explain how this "steady state" arises, and also to establish whether the economy is able automatically to return to this state and to maintain it.

It turned out that different answers were given to these questions by the various schools because of their different assumptions about the functioning of the capitalist economy and the different ways in which they defended capitalism.

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[1] The American economist R. Solow says: "Most of the modern theory of economic growth is devoted to analysing the properties of steady states and to finding out whether an economy not initially in a steady state will evolve into one if it proceeds under specified rules of the game." (R. M. Solow, *Growth Theory. An Exposition*, Clarendon Press, Oxford, 1970, p. 4).

The Keynesian theory of growth approached both groups of problems on the basis of the Harrod-Domar equations, in which the rate of national income growth was determined by two factors: the rate of accumulation and the size of the "capital-product" ratio, it being assumed that this ratio is rigidly fixed by the technological conditions which rule out the possibility of any flexible substitution of production factors. And because technical progress, according to the accepted premise, is neutral, the "capital-product" ratio has a tendency to remain constant. That is why the rate of accumulation was regarded as the crucial and virtually the sole parameter determining the potential growth rate.

As for the second group of problems—steady state and the mechanism for its maintenance, that was examined by Keynesian theory in a light highly unfavourable for capitalism.

First, it drew a distinction between two "steady states": one corresponding to full employment ("natural growth rate") and the other meeting the interests of business but not necessarily entailing full employment ("guaranteed growth rate").

Second, and that is the main thing, neither of these two states, according to Keynesian theory, constituted a truly steady dynamic equilibrium. The actual growth rate could only accidentally coincide with one of these, with the result that the whole system was subjected to short-term and protracted departures from the state of equilibrium and for that reason needed to be regulated by the government. This conclusion was drawn on the basis of Keynesian growth models in complete accord with the views held by Keynes and his followers about the imperfection of the capitalist economy and its serious defects, which called for government intervention to maintain the necessary economic proportions.

The neoclassical approach was a totally different one. Fixed capital and labour power, capable of combining in various proportions under the impact of technological and economic factors, came to be regarded as the primary macroeconomic factors of growth. The factor of scientific and technical progress was introduced into analysis as summing up the influence exerted by science, education, and organisation for enhancing the efficiency of production factors.

This approach, together with the use of the apparatus of production functions and empirical evaluation of its parameters yielded a number of interesting conclusions concerning the role of individual factors in the capitalist countries' economic growth, notably, the tremendous contribution now being made to growth rates by scientific and technical progress and its individual components.

But neither these calculations, nor the use of the production function are the essence of neoclassical theory.

The production function can merely express the quantitative relationships between input and output, without containing any other qualitative element. "Engineering" production functions can be constructed for individual types of product (which will then reflect the technological specifics of the given line of production). They can also be constructed for the national economy as a whole, through a definition of their parameters on the basis of dynamic series or other indicators. Such functions are used for analysing existing quantitative relationships, for estimating the role of extensive and intensive factors of growth, and in forecasting.

But the production function, used as a mathematical expression of neoclassical growth theory, contains something more than a mere expression of the existing quantitative relationships between input and output. It is assumed that the relationships between these connections in the neoclassical production function are an expression of the state of economic equilibrium. This function implies and expresses, alongside the technological relations, the socio-economic relations of distribution under full employment of economic resources. Only with this kind of "filling" does the production function acquire the quality of a neoclassical growth model and become a form embodying the substance of the neoclassical theory of growth and distribution.

The premises of the neoclassical production function as an economic growth model boil down to the following main propositions:

1. Labour and capital are the two homogeneous production factors which create a homogeneous product.

2. Free competition has full sway, as a result of which the income going to each of the production factors accords with their marginal products, i.e. wages are equal to the marginal product of labour, and profit (interest) is equal to the marginal product of capital. That is why the distribution of income simultaneously expresses the production contribution made by each of these factors to the value of the product.

3. Free competition and unhampered substitution of labour and capital, and also the free change of the prices of production factors in accordance with the dynamic of labour and capital ensures the full employment of all the resources.

4. The unconsumed part of the product (i.e. savings) is invested, and there is no problem of demand.

5. The growing scale of production does not influence the growth of efficiency; where the mode of production remains unchanged, factor productivity tends to decline.

6. Technical progress is neutral and autonomous, equally enhancing the efficiency of all the factors of production.

7. The elasticity of production factor substitution is equal to unity; in other words, a change in the relation between profit and wages causes a precisely similar change in the relation between labour and capital, and vice versa. For that reason, the distribution of income does not change.

8. Capital is homogeneous and operates as a uniform, "malleable", "jelly-like" mass capable of flexibly responding to any changes in the relation between the prices of production factors.

An analysis of these premises reveals the flimsy foundation on which the neoclassical models of economic growth are based.

The first four points listed above relate to a characterisation of so-called enterprise equilibrium, and do not stand up to criticism in the light of the actual facts. The premise that the factors of production are homogeneous is extremely oversimplified. The reign of free competition is a thing of the long distant past. The mechanisms for establishing a temporary equilibrium within the capitalist system, with its powerful monopoly organisations and state regulation, and with the unionised working class capable of resisting monopoly pressure on wages, have become much more complicated. The processes of economic adjustment are effected not so much with the aid of prices as through changes in the volume of production and the degree of use of production capacities.

So, the assumption that free competition is the mechanism which, through a change in prices, brings the conditions of production and the conditions of distribution into equilibrium is totally unrealistic and merely serves to vindicate capitalism.

There is a fundamental flaw in the very concept that capital has "productivity" and that the marginal products and "prices" of production factors are equal. That the theory of marginal productivity is untenable was shown in the early works of I. G. Blyumin[1], and also in the works of L. B. Alter.[2] Labour alone creates new value. Capital as a stock of value does not create any new value but merely provides a condition for the creation and appropriation of value. Blyumin said, for instance, that

> "the theory of the productivity of capital is based on a gross confusion of the material and value elements. The main argument behind this theory is that the means of production (mainly the instruments of production) are capable of increasing the quantity of the product, i.e. the quantity of use values. This is used as a basis for the apologetic conclusion that capital is capable of producing new values and, consequently, surplus value."[3]

The confusion of physical and value elements produces serious discrepancies in the inner logic of neoclassical theory and these together with its logical inconsistencies explain the profound criticism to which that theory has been subjected within the framework of non-Marxist political economy and the consequent discussions of value, its origins, distribution, etc. These discussions showed, among other things, that a logically consistent theory of distribution cannot be based on the theory of marginal productivity, because any measurement of the "marginal product of capital" entails a measurement of the "value" of capital, and the latter, for its part, turns out to depend on distribution categories. Consequently, the theory rotates in a vicious circle.

Points 5 to 8 listed above refer to the specific features of technical progress which give ground

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[1] See: I. G. Blyumin, *A Critique of Bourgeois Political Economy*, Vol. 1, USSR Academy of Sciences Publishing House, Moscow, 1962 (in Russian).

[2] See: L. B. Alter, *Bourgeois Political Economy in the United States*, Sotsekgiz, Moscow, 1971 (in Russian).

[3] I. G. Blyumin, *op. cit.*, pp. 319-320.

for defining it as neutral. Here again the assumptions are extremely tentative. Their use may be justified over a short period for assessing the role of technical progress and its "contribution" to economic growth, but these premises turn out to be unrealistic for an analysis of the long-term effects of technical progress on economic growth.

The statistical variant of the Cobb-Douglas function accorded with the above-mentioned premises:

$$Y = AK^{\alpha}L^{\beta}.$$

With the introduction of the indicator of neutral technical progress, this function assumed the following form:

$$Y = AK^{\alpha}L^{\beta}e^{rt},$$

where Y is the product; K and L are the inputs of capital and labour resources; α and β, respectively, the elasticities of capital and labour; and rt, the rate of neutral technical progress.

Since this function was introduced into theoretical and statistical literature, its life has undergone a dichotomy. On the one hand, it is broadly used in empirical calculations for evaluating the role of individual factors of economic growth, especially in assessing the role of technical progress. On the other hand, it is used (on the strength of the assumptions examined above) for a vulgar and apologetic interpretation of dynamic equilibrium problems and the problem of distribution. These two aspects of its use should not be confused.[1]

The neoclassical model is designed to prove that the capitalist economy has internal stability and has all the necessary mechanisms for automatically

[1] The assumptions of neoclassical theory leave their imprint on empirical analysis only when magnitudes characterising the distribution of the national income between labour and capital are taken as α and β indicators; or, conversely, when empirically established α and β are identified with the indicators of national-income distribution.

re-establishing the distorted equilibrium. Thus, the British neoclassic J. E. Meade[1] has shown that the neoclassical model of the economy in the form of the "Cobb-Douglas function" has a tendency towards a "static equilibrium", i.e. in this model all the basic economic magnitudes (income, capital, savings, investment) tend to grow at stable rates equal to the rate of labour power growth. Whenever any destabilising factors cause an acceleration or slowdown in the growth of savings (and, consequently, of the rate of capital accumulation), the latter, according to the neoclassics, will not influence the rate of income growth, so causing its acceleration or slowdown, but will change the "capital-labour" ratio, or the "capital-product" ratio. Because of the elasticity of prices or flexible monetary policy, this will change the ratio between profit and wages, leaving the distribution of income and all the other growth indicators unchanged. QED: equilibrium turns out to be stable.

As has been said above, however, the assumptions on which this model is structured are a far cry from reality, which is why its functioning cannot reflect the essentials in the functioning of the existing capitalist economy. But we find that even more complex types of neoclassical production functions are keynoted by the same idea that the capitalist economy is intrinsically stable. From these also follow the practical conclusions concerning the scale and instruments of government intervention in the economy. According to the neoclassics, such intervention should be kept down to a minimum and confined to the sphere of credit and money regulation.

The subsequent development of neoclassical growth theory has been characterised by some changes and complexifications in the assumptions of anal-

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1 See: J. E. Meade, *A Neo-Classical Theory of Economic Growth*, George Allen & Unwin Ltd., London, 1961.

ysis which take into account some of the actual aspects of economic growth. In this context, one could note two main lines in the evolution of this theory.

One of these is connected with the introduction of the money factor into analysis as a key element of the economic system explaining why there are economic fluctuations despite the fact that the system has a tendency towards a "steady state". This line has led to the monetary theory in the formation of the national income and the cycle in contrast to Keynesian theory.[1]

The second line is connected with a change of premises characterising technical progress and its impact on economic growth. This line in the modernisation of the neoclassical theory of growth is examined below. Let us note, at this point, that the introduction of the money factor into analysis (in spite of the one-sided evaluation of its role) and the urge for a finer analysis of the nature of technical progress and the elaboration of a formal apparatus for characterising its individual aspects contained a number of positive elements which helped to understand capitalist reproduction.

One should also emphasise the following. The evolution and modernisation of neoclassical theory has not in any sense discarded the assumptions which were characterised as "conditions for business equilibrium". The theory is still based on the premise of the free play of competition and of the prices of production factors being established in accordance with their marginal products determining the distribution of the national income, and the absence of any problem of realisation. Despite the fact that these premises have long been subject to criticism by some Western economists, they still constitute the basis of the neoclassical models of growth.

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[1] This line is examined in the next chapter.

If a distinction is drawn between two aspects of neoclassical analysis—the analysis of supply (or the aspect of production) and the analysis of the mechanism by means of which the economy adjusts to the changes in supply (the balancing out of supply and demand)—we find that corrections have been made only in the former aspect, while the latter has not, in effect, been modified: free competition and the movement of relative prices (sometimes with the aid of the monetary policy) bring demand into accord with supply.

For all these reasons, the neoclassical theory of growth, despite all its modernisations and corrections, which were made in the course of its subsequent evolution, is still a far cry from the scientific analysis of the key features of the actual process of capitalist reproduction.

2. Development of the Neoclassical Theory of Technical Progress

As it has been said above, the development of the theory of scientific and technical progress and a deeper analysis of its impact on economic growth has been the main line in the evolution of neoclassical theory.

It gives a very broad definition of scientific and technical progress, not only as qualitative changes in the economy resulting from the improvement of hardware and technology, but also as improvement in organisation and as rising standards in the training and education of labour power. It was initially introduced into the Cobb-Douglas function as a time factor, in order to explain that part of the product increment which could not be explained only through the growth of physical inputs of labour and capital. Subsequent analysis of the impact of scientific and technical progress on economic growth involved the elaboration of a more differentiated system of quantitative indicators of technical progress, reflecting not only the general influence of scientific and technical progress on economic growth, but also its differentiated impact on the efficiency of the individual growth factors and its influence on the extent of economic resources substitution. These characteristics were used to develop a general theory of technical progress and advance to more complex types of production functions.

Neoclassical theory refers the following concepts to the characteristics of technical progress:

1) efficiency of technical progress;
2) economies of scale;
3) labour or capital intensity of technology;
4) elasticity of substitution of labour and capital.

One could say that the classification of technical progress indicators (abstract technology) provides a useful set of instruments for *empirical analysis* of the impact of technical progress on economic growth, empirical analysis effected through production functions. But the neoclassics believe that its results back up the laws of the theory of marginal productivity and the functional theory of distribution which is based on these laws. That is why, when considering these problems, it is especially important to separate the aspects of quantitative analysis which are of practical use, from their vulgar and apologetic interpretation.

There are no special objections to the interpretation of the characteristics of neutral technical progress. With certain assumptions these could be taken as tentative gauges of its contribution to economic growth, and also as indicators of the aggregate efficiency of production factors. They can be obtained through different modes of verification of the Cobb-Douglas function.

It is more difficult to obtain characteristics of non-neutral technical progress, where two indicators have the key role to play: elasticity of substitution (σ) and capital intensity, which is measured as the ratio of the shares of production factors in the product (α/β).

Let us consider in detail how the concept of substitution elasticity is interpreted in neoclassical theory. In concrete calculations, σ is measured as a coefficient characterising the change in the capital-labour ratio (K/L), depending on the changing correlation of their prices, i.e. profit and wages: $\sigma = E\ (K/L)/E\ (w/p)$. For instance, the higher the price of labour, the higher are the wages and the greater the incentive for substituting capital for labour, and so the higher the K/L ratio. If there are no technical or socio-economic obstacles to such a substitution, and if the efficiency of the production factors tends to change similarly, then $\sigma = 1$. Where something hampers such a substitution, or a unit of one and the same factor requires, for technical reasons, a much greater or lesser use of the other resource, then σ is greater or less than 1 ($\sigma >< 1$).

So, there is some practical interest in measuring the magnitude of substitution elasticity. However, once we have this magnitude, we can still say nothing about which factors have determined its given level.

The point is that the peculiarities of technology are among the determinants of the proportions in factor substitution under the influence of changes in their prices or obstacles to such substitution.

But there are other, socio-economic and political, factors, which also can and do influence the magnitude of this ratio. Among them are trade union policy, government intervention, traditions, obstacles to the migration of labour, inflexible price formation, the policy of the monopolies, etc. These factors also need to be taken into account in an analysis of the factors determining substitution elasticity on the scale of the economy as a whole, for the reduction of all the causes to the peculiarities of technical progress tends to distort the characteristic of technical progress itself. That is why, while not denying the interrelationship itself and recognising the usefulness of its quantitative analysis, we believe that the factors which determine its level cannot be reduced to the specific features of technical progress alone.

If magnitude σ is to convey the specific features of technical progress, there is a need, on the strength of the basic theoretical premises of neoclassical theory, first, to recognise the existence of free competition and the absence of any socio-political factors engendering various "inflexibilities" in the economic system; second, to accept that profit and wages are equal to the marginal products of the corresponding production factors; and third, to regard capital as homogeneous. Only then will σ testify to the character of the K/L ratio and of their marginal products (as expressed in the ratio of p and w).

$$F_K = \frac{\delta Y}{\delta K} \text{ and } F_L = \frac{\delta Y}{\delta L}$$

then

$$\sigma = E\ (K/L)/E\ (F_K/F_L).$$

If, for instance, the marginal product of labour tends to rise faster than the marginal product of capital (in consequence of the accumulation of production experience), then a substitution of a unit of labour will require several units of capital and $\sigma > 1$. Only with these assumptions can substitution elasticity reflect the specific features of technical progress, which consists in the fact that the efficiency of production factors tends to grow unequally: the efficiency of one of them tends to grow faster and its contribution to economic growth, more tangible (the labour process becomes more labour intensive or more capital intensive). Such an interpretation is a logical one on the strength of the accepted assumptions.

But these assumptions themselves, as it has been noted above, do not accord with reality, which is why substitution elasticity, measured empirically as a relation between the rate of change of the capital-labour ratio, and that of the wages-profit ratio does not provide a reliable enough indicator of the type of technical progress.

One could evidently judge much more authentically about the type of technical progress only on the basis of purely empirical calculations of the α/β ratio over long periods of time.

The neoclassics identify these coefficients with the distribution of the national income between the main classes of society, believing that the dynamics of the distribution indicators can provide evidence of this or that type of technical progress: for instance, the growth of labour's share indicates the labour-intensive type, and vice versa. But if the neoclassical premise concerning the equality of the marginal products and the prices of production factors is discarded and the change in α/β is determined on the basis of a purely empirical analysis, the data so obtained will reflect the influence of the non-neutral type of technical progress.

An increase of one coefficient as compared with the other will testify to a growth of its efficiency and of its influence on economic growth. Conversely, a reduction of the other will testify to a decline of its influence on economic growth.[1]

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[1] In this context, interest attaches to the statistical approach in analysing the α/β ratio, as worked out by Murray Brown in his book *On the Theory and Measurement of Technological Change*, London, Cambridge University Press, 1966. The author based his analysis on the US economy from 1890 to 1960, a period he divided into technologically homogeneous segments of time, and reached the conclusion that up until the 1920s, technical progress was capital-intensive (α/β grew) and since the 1920s, it has been labour-intensive (α/β declined) (*Ibid.*, p. 149).

An interesting analysis showing the distinctions in the influence exerted by the rate of growth of resources (labour and capital) on the rate of product growth (with various

So, while recognising the usefulness of the apparatus for analysing technical progress, we believe that it is necessary to re-emphasise that it is applicable only within the framework of a purely *empirical* approach to the problem. There is good reason why the growing potentialities for modelling technical progress, the elaboration of mathematical formalism for its analysis, and a system of quantitative characteristics of technical progress stimulated the development in this area of empirical studies which are of unquestionable practical interest. These studies were connected with the elaboration of a concept of endogenous technical progress, whose rate and level are determined by factors within the economic system. Hence the problem of expressing these factors in concrete terms and working out the methods for their quantitative analysis. The inputs into education, science, research and development, and the extension and application of new knowledge are the elements of the inputs which came to be analysed as the factors determining technical progress.

Closely bound up with the solution of this problem was another line of this analysis, the problem of embodiment, or materialisation, of technical progress, because it is quite obvious that most qualitative changes in the economy are embodied in more skilled and experienced labour power, employing improved equipment, etc.[1] This line of

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α/β ratios) has been given by A. Kandel in a paper entitled "Accumulation and Rates of Economic Development" in the journal *Mirovaya ekonomika i mezhdunarodnyie otnosheniya*, No. 6, for 1972.

[1] The author of a survey of economic growth theory is quite right in saying that "in principle, if all the inputs are properly measured and the function governing their interactions is precisely specified, then the residual dA/A should be zero or nearly so." (M. Ishaq Nadiri, "Some Approaches to the Theory and Measurement of Total Factor Productivity: a Survey". In: *The Journal of Economic Literature*, Vol. VIII, December 1970, No. 4, p. 1150.)

analysis produced interesting statistical methods for evaluating and recording qualitative changes in inputs, and stimulated the elaboration of models of embodied, or materialised, technical progress.

There were also numerous studies in a more precise measurement of inputs, especially of capital, since the statistical methods used in calculating it are still extremely imperfect. The many shortcomings in evaluating the magnitude of capital are regarded as the reason for which the size of capital's "contribution" to economic growth is being understated. An interesting approach to the evaluation of capital entailed the assumption that each new "generation" of the means of production has a higher productivity, so that when the total magnitude of capital is calculated each subsequent "generation" of the means of production should be given a greater weight. As a result, such calculations also ascribe a much higher "contribution" by capital to economic growth. Meanwhile, the overall "contribution" by technical progress is divided into that which is not materialised and that which is materialised in capital formation. This approach was first proposed by Solow back in 1962.[1]

Consequently, there is evidence of some advance in the *quantitative* methods of technical progress analysis, but this does not apply either to the theoretical interpretation of technical progress itself on the strength of the general premises of neoclassical theory, or to the theoretical interpretation of models including various types of technical progress.[2] This applies especially to the neoclassics'

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[1] See: R. M. Solow, "Technical Progress, Capital Formation, and Economic Growth". In: *The American Economic Review*, Vol. LII, May 1962, No. 2.

[2] Bourgeois economists themselves admit that the unrealistic and narrow premises on which the neoclassical theory of technical progress is based are unsatisfactory. The theory fails to provide solutions for some vital problems now facing students of technical progress.

use of concepts concerning the types of technical progress for "modernising" the neoclassical theory of distribution.

3. Scientific and Technical Progress and the Problem of Distribution in Neoclassical Theory

The neoclassical theory of economic growth, as it has been said, claims to be simultaneously a theory of distribution. The neoclassical production function is a formal expression of a concept of economic equilibrium in which production and distribution have been balanced out to meet the conditions for maximising profits.

Let us consider in greater detail the content and evolution of this theory, specifically as a theory of national income distribution. Let us recall that it is based on the theory of marginal productivity, according to which the income of each production factor (labour, capital, and land) is determined by its "price". The latter, for its part, is proportional to the marginal product. *The price of the production factor* and its quantity (i.e. supply) also determine its share in the aggregate social product.

So, this theory switches the whole great and multifaceted problem of distribution into the sphere of microeconomic conditions in which the prices of production factors are formed, and this, in effect, does away with the relatively independent problem of distribution, which is converted into a purely technical process ensuring the receipt by each production factor (through the corresponding mechanism of price formation) of its product.[1]

[1] In this context, Robert Lekachman wrote: "After the 1870s economics became an increasingly refined mode of valuation, in which the marginal principle constituted a complete exposition of how economic resources were allocated and how individual wants set the process in motion." (Robert Lekachman, *A History of Economic Ideas*, Harper & Brothers Publishers, New York, 1959, p. 175).

Let us note that even in the 1930s, this theory hardly satisfied anyone. That was the period in which criticism began of the fundamental premise of neoclassical theory, namely, free competition, which had given way to various forms of monopoly competition determining the actual price formation of products and production factors.

The inclusion of production functions into the theory of distribution under the high auspices of mathematics gave this decrepit theory a shot in the arm just as its unrealistic assumptions were being made increasingly obvious.[1]

What was the significance for the neoclassical theory of distribution of the introduction into analysis of the Cobb-Douglas function in its initial form and in its modernised version with the inclusion of the technical progress factor?

The fact that this function gave a good description of the statistical interrelationships between the dynamics of product, labour and capital was seen by its advocates as empirical evidence of at least two of its basic postulates:

first, factor prices correspond to their marginal products (this postulate was allegedly borne out by the fact that the obtained parameters of distribution or elasticity of income for labour and capital (α and β) were roughly equal to the corresponding shares of wages and profits in the national income;

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[1] Replying to the question of why the theory of marginal productivity had such a staying power (despite the fact that no one any longer believed in free competition and sustained equilibrium), Tibor Scitovsky wrote: "For one thing, its generality and elegance has considerable appeal; for another, it fits in best with our marginalist approach to economics; for a third, the acceptance of the marginal productivity theory of income distribution is closely bound up with the assumption of an aggregate production function whose analytic convenience has enticed many economists to slur over or disregard the objections to it." (*The Behavior of Income Shares. Studies in Income and Wealth*, Vol. 27, Princeton University Press, Princeton, 1964, p. 22).

second, the dynamics of production factors (K and L) and their marginal products, and consequently, their "prices" (p and w) were in inverse and straightforward proportion, i.e. the growth of the capital-labour ratio (K/L) was connected with a corresponding decline in the ratio of profit to wages (p/w).

The fact that the function with constant parameters of distribution (for in the Cobb-Douglas function α and β are constant) corresponded to the actual data warranted the conclusion that the relation between the rate of K/L growth and the rate of p/w decline (i.e. substitution elasticity) was equal to unity. This meant that any change in the relation between the volume of production factors was compensated by corresponding changes in the relation between their "incomes", and that an increase in the stock of capital with respect to labour would lead to a reduction in profit with respect to wages. As a result, the share of this factor in income would not change. In this way, the Cobb-Douglas function was used to substantiate in theory the *constancy of national income distribution over the long term.*

Let us recall that constancy of distribution was one of the "stylised facts" which economic growth theory had to explain and substantiate. But actual economic development tends to depart from these stylised facts, and frequently clashes with them. This also applies to the long-term trends in the "capital-product" ratio and national income distribution.

How are these departures to be explained without upsetting the principles of neoclassical theory?

An effort to salvage the theory, and above all to explain the important socio-economic problem of distribution was made by means of the concept of non-neutral technical progress.

Formal evidence that the neoclassical theory of production and distribution is untenable comes from the fact that it did not allow for, and so failed to explain, possible changes in national income distribution. If changes in the rate of growth of production factors go hand in hand with corresponding changes in their marginal products and, consequently, in their "prices" (for instance, a relative growth of capital, says the theory, leads to a relative decline in profit), then there should be no changes in income distribution. But if national income distribution does change, this means that the laws of marginal productivity do not work. That is precisely the conclusion some bourgeois critics of the theory have drawn.

But present-day champions of the neoclassical theory of production and distribution seek to prove that these changes could be connected not with a disruption in the operation of the laws of marginal productivity, but with the influence of the type of technical progress and the magnitude of resource substitution elasticity.[1]

According to the neoclassical theory of non-neutral technological change, the redistribution of income in favour of profit and an increase in the share of the latter in the national income can occur in two cases:

if technical progress is capital-intensive, because the marginal product of capital and, accordingly,

[1] Murray Brown writes, for instance: "There are two propositions in the neoclassical tradition which hold that relative shares are the resultant of configuration of non-neutral technological change, the elasticity of substitution and the labour-capital ratio. The first holds that a factor-saving innovation, *cet. par.*, reduces the relative share of income of that factor in all cases. The second maintains that if one factor increases in supply more rapidly than another, and if the elasticity of substitution (σ) is less than unity, then the relative share of the first factor decreases. Of course if σ exceeds unity, then the relative share of the first factor increases; and if σ is equal to unity (the Cobb-Douglas case), changes in the relative supplies of factors will have no effect on the relative shares." (Murray Brown, *On the Theory and Measurement of Technological Change*, Cambridge University Press, London, 1966, p. 181).

the rate of profit, tend to grow faster than the marginal product of labour and wages;

if the magnitude of capital grows faster than the size of the population ($k > l$), but the elasticity of substitution is so high ($\sigma > l$) that the marginal product of capital and the rate of profit decline insignificantly relative to wages; or, conversely, if capital grows slower than the population, but substitution elasticity is hampered ($k < l$), so that the marginal product of labour and the level of wages decline markedly relative to the rate of profit.

A converse line of reasoning should explain the redistribution of income in favour of labour and a growth in the share of wages in the national income. The opposite impact of these two effects, according to the theory, would leave distribution unchanged.

Thus, the neoclassical approach to explaining changes in national income distribution rests on the impact of two effects: the effect of technological change itself, and the effect of resource substitution. But in reality it is impossible, for all practical purposes, to measure separately the impact of these two effects. It is possible to measure substitution elasticity as the relation between the changing capital-labour ratio and the wages-profit ratio. However, first, as it has been said, this relation is not at all identical with the relation between the dynamics of resources and their marginal products. Second, even if that were so, we are incapable of establishing what has determined the concrete given relation between K/L and w/p: is it the type of technical progress which has a direct impact on the relation between the marginal products, or the difficulties in the very process of substitution in consequence of differing accessibility of resources?

In other words, there are substantial defects in the theory of technical progress itself, and these hamper the concrete expression of the techno-economic factors which allegedly determine the processes of distribution.

CHAPTER TWO

THE PRESENT STAGE OF THE "ANTIMARGINALIST REVOLUTION" AND KEYNESIANISM

The neoclassical theory of technical progress, while having somewhat refurbished the theory of distribution, failed to eliminate its basic flaw, namely, the idea that the incomes of the factors of production are determined by their marginal products. This idea was used by the advocates of the theory of functional income distribution to obscure the socio-economic nature of distribution, which is determined by the relations of exploitation and the sharp class struggle, and which is closely connected with the basic proportions of reproduction in capitalist society.

This makes all the more interesting the ongoing discussion within bourgeois economics on the neoclassical theory of growth and distribution, especially its basic postulates. The sharp tone of this discussion, with the far-reaching conclusions being drawn with respect to the fundamental methodological positions of bourgeois economics and the need for fresh approaches to its development show that neoclassical theory, despite all the "improvements" it has undergone in the course of its evolution, is in a state of grave crisis. It is now being sharply criticised by various groups of bourgeois economists.

This chapter considers the views of the most influential group of its critics, the economists of the Cambridge School (Britain), who have had an especially important role to play in toppling the pillars of neoclassical theory and who want bourgeois economics revamped, and its theoretical apparatus renewed. The leading members of this group are Joan Robinson, Piero Sraffa and Nicholas Kaldor.

The protest against the neoclassical line in bourgeois economics has a fairly long history behind it. It was first criticised by the institutionalists. The stages in the history of the struggle against the neoclassical line in bourgeois economics have been marked by the rise of Keynesianism, with its ideas of government regulation of the economy, the spread of the theory of monopoly and monopoly competition, and the use of this theory in analysing price formation problems and the functioning of markets.

Back in the 1920s, Sraffa criticised the neoclassical theory of price and declared that its initial premises were unrealistic. There was substantial criticism of these premises (above all, of the idea of the reign of free competition and the optimising role of the market mechanism) in the 1930s, with the publication of works by E. H. Chamberlin and Joan Robinson substantiating the theory of monopoly competition and the theory of "imperfect" competition.

In these spheres of analysis, the neoclassical trend gave way to Keynesianism and neo-Keynesianism, the theory of monopoly competition, analysis of market structures, etc.

But, while having adapted itself to the analysis of economic growth problems, neoclassical theory simultaneously maintained its positions as the theory of the creation of value, and the theory of distribution of the national income between labour and capital.

The current "antimarginalist revolution" has run precisely towards these spheres of neoclassical domination constituting an important citadel of bourgeois apologetics. What is more, one can now say that the radical wing of bourgeois economics has taken shape as an independent school opposed to "orthodox" theory and exerting, in particular, a tremendous influence on the economic theories of "leftists" of every stripe, above all, on radical economics. For the time being it has no generally accepted name and, with some reservations, could be designated as "left Keynesianism". Its spokesmen call it "post-Keynesianism".[1] But whatever its name, these are its main features:

—sharp criticism and rejection of the basic propositions of the neoclassical school, above all of its theory of marginal productivity and theory of marginal utility;

—revival of some traditions of classical bourgeois political economy in the form of Recardianism;

—recognition of Marx's theoretical contribution to the analysis of capitalist reproduction; and

—reappraisal of the basic categories of bourgeois economics: value, capital, profit, distribution, etc.

The publication of Joan Robinson's *The Accumulation of Capital*[2] and some of her articles, especially "The Production Function and the Theory of Capital",[3] was something of a milestone in the development of this trend. A new chapter in the history of "the antimarginalist offensive" was opened by Piero Sraffa[4]. All these works started major

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[1] See: J. A. Kregel, *The Theory of Economic Growth*, Macmillan, London, 1972.

[2] See: J. Robinson, *The Accumulation of Capital*, Macmillan & Co. Ltd., London, 1956.

[3] See: J. Robinson, "The Production Function and the Theory of Capital". In: *The Review of Economic Studies, 1953-54*, Vol. XXI (2), No. 55, pp. 81-106.

[4] See: P. Sraffa, *Production of Commodities by Means of Commodities. Prelude to a Critique of Economic Theory*, Cambridge University Press, 1960.

discussions in Western economic literature which are in progress to this day.

1. Criticism of Neoclassical Dogmas

Robinson and Sraffa criticised two main dogmas of the neoclassical theory of production and distribution:

—Dogma No. 1: the incomes of the factors of production and their distribution can be derived from the conditions of their supply and their "productivity"; and

—Dogma No. 2: there is a simple relation between the correlation of production factors and their incomes, so that an increase in the capital-labour ratio (K/L) necessarily leads to a reduction in the rate of profit (p), and vice versa.

Dogma No. 1 has long been under fire from the opponents of the neoclassical theory of distribution. The substance of the criticism is that the supply of production factors and their measurement are influenced by the relations of distribution, and that is why neoclassical theory finds itself in a vicious circle.[1]

Central to this criticism is the measurement of the physical magnitude of capital. Can it be measured regardless of the categories of distribution? The neoclassics start from such an abstract pos-

[1] Two US economists write: "The most obvious criticism, which has been made over and over for decades (and continuously ignored) is that the demand for commodities and the supply of factors are significantly influenced by the distribution of income. This involves a circularity from which the theory, on the micro-level, could never escape. Nevertheless, the theorists did not hesitate to aggregate the categories of marginal productivity distribution theory in order to provide a macroeconomic ideology justifying the class distribution of income between profits and wages." (E. K. Hunt and Howard Sherman, "Value, Alienation, and Distribution". In: *Science and Society*, Spring 1972, Vol. XXXVI, No. 1, p. 42).

sibility, but their opponents claim that it is impossible.

According to neoclassical theory, the volume of capital is usually determined as capitalised income, depending on the interest on a stock of capital assets (which is identified with the rate of profit in conditions of equilibrium). Consequently, if the value of capital assets is to be determined, the rate of interest must be known in advance. Meanwhile, this theory claims to explain the formation of production-factor incomes, including the rate of interest.

This circularity was subjected to full-scale criticism by Joan Robinson.[1] She said that it was impossible to find a unit for measuring capital that would not depend on relative prices and relations of distribution. The prices of capital goods, by means of which this whole heterogeneous mass is reduced to a single whole, include profits and wages. A change in the relation between them has an effect on prices and the volume of capital, without bearing, in effect, on its physical properties and "productivity". That being so, the theory which claims to explain the laws of distribution by means of factor "productivity" is not entitled to operate with price indicators.

This idea was spelled out in greater detail and strict mathematical terms by Sraffa in the abovementioned work. Considering the process of social reproduction and price formation on the basis of schemes of the circulation of goods, Sraffa, first, gave a new approach to computing the volume of capital on the basis of the prices of production of that total of intermediate goods which are used for making the end product. Second, he demonstrated that the latter (when calculated on the basis of the prices of production) is influenced by

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[1] See: J. Robinson, "The Measure of Capital: The End of Controversy". In: *The Economic Journal*, September 1971, No. 323, Vol. 81, pp. 597-602.

distribution: a change in the relation between profits and wages tends to change the prices of production and, through these, the magnitude of the value of capital measured on the basis of these prices of production.

That was how Sraffa and Robinson criticised Dogma No. 1 of the neoclassical theory of production and distribution.

Let us now consider the criticism of Dogma No. 2.

A fundamental proposition of neoclassical theory is that there is a simple connection between the capital-labour ratio and the correlation between profits and wages.

What will be the effect of a change in this correlation?

Neoclassical theory asserts that if there is an increase in the correlation between wages and profits (a relative decline in the rate of profit) labour will be substituted by capital, i.e. there will be a switch to more capital-intensive methods of production.

Sraffa proved that that was not true. The point is that neoclassical theory assumes capital to be a homogeneous mass, with the whole of it consisting of stocks having the same period of circulation, the same starting dates, the same efficiency, etc. Only this kind of "jelly-like", "malleable" capital can lend itself to ceaseless substitutions under a changing correlation between the prices of production factors. Sraffa proved that once the premise of the homogeneity of capital was rejected, that dogma of neoclassical theory also collapsed.

Discussions of this problem among bourgeois economists went forward in connection with the "switches of techniques" effect, discovered almost simultaneously but independently of each other by Robinson and Sraffa.

Both started from the assumption that there was no smooth and ceaselessly differentiated production function. Instead, they suggested that the production function should be regarded as a range of all the possible combinations of production inputs (which for technological reasons may not be all that many), and the resultant outputs. It was then discovered that one and the same rate of profit could correspond to different capital-labour ratios and vice versa.

Sraffa proved this with his goods-circulation schemes characterising a vertical cross-section of their production. If the production process is considered in time with an eye to its stages, each of which is characterised by a different capital-labour ratio, this or that production technique could be made optimal by changes in the rate of profit. As a result, a reduction in the rate of profit could induce a switch to a new and more capital-intensive production technique or, on the contrary, a return to an older and less capital-intensive technique, a proposition neoclassical theory had never allowed.

Sraffa's main point, consequently, was that it was impossible to deduce any definite relation between the capital-labour ratio and the profit-wages ratio.[1]

But if the capital-labour ratio and the rate of profit are not so rigidly related to each other as neoclassical theory suggests, the link is disrupted

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[1] One of Sraffa's associates, Luigi L. Pasinetti, gives a visual example of how under two different techniques of production, a gradual rise in the rate of profit makes it more profitable to switch from one technique to another, and at a certain point makes for a return to the former: "The general conclusion is that, at any given state of technical knowledge, switches of techniques due to changes in the rate of profit do not allow us to make any general statement on changes in the 'quantity of capital' per unit of labor. The new technology may require a lower 'quantity of capital' per unit of labor, or it may require a higher 'quantity of capital' per unit of labor." (L. Pasinetti, "Changes in the Rate of Profit and Switches of Techniques". In: *The Quarterly Journal of Economics*, Vol. LXXX, November 1966, No. 4, p. 514.).

between the marginal products of the factors and their prices, the link on which the whole of neoclassical theory of income distribution rests.

Many economists believe that the criticism of the premise of capital homogeneity and the description of the "switches of techniques effect" were crucial in toppling the whole of the neoclassical theory of distribution.[1]

We think that bourgeois economists tend to overrate the results of this "revolution", when they say that the critics of the "marginalist" concept adopt Marx's theory of exploitation in their efforts to find new explanations for the factors which determine distribution. That would require recognition of Marx's theory of value and surplus value, and this is precisely something that none of them has done. The whole of this criticism has been carried on from the standpoint of production costs and formation of production prices, be it a matter of measuring the volume of capital or of factors determining the "switches of techniques".

That is a fundamental feature of the approach taken by Robinson, Sraffa, and their followers, and this tends to limit the importance of their contribution to a positive elaboration of the problems they tackle. But in terms of the impact of their criticism on the disintegration of the "marginalist" theory of distribution, it was, indeed, highly significant, and provided important evidence of the crisis of one of the traditional doctrines which had dominated bourgeois political economy for nearly a century.

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[1] "Although the arguments were very esoteric, the general principles established are rather simple and are of monumental importance in the history of economic doctrines. They represent the logical and theoretical destruction of the intellectual tradition, going hack to Jevons and the Austrians which has dominated orthodox economics for the last 100 years." (E. K. Hunt and Howard Sherman, *op. cit.*, pp. 44-45.)

2. Theory of Value and Price Formation. Discussion of Sraffa's Work

In place of the neoclassical theory, the post-Keynesians adopted a peculiar version of the Ricardian theory of value, price formation and distribution, which emerged on the basis of Sraffa's abovementioned work. Some even tried to interpret that theory as a Marxist one or to use it to "enrich" or "develop" the Marxist theory of value and distribution.

These attempts led to acute disputes and disagreements, but they also attracted much attention to the Marxist theory of value, especially to that aspect of it which is connected with the problem of the conversion of value into the price of production, that is, to the transformation problem. That is why it is so important to analyse Sraffa's theory as such, and in comparison with Marxist theory.

What is the substance of Sraffa's theoretical system? What are the specifics of its methodology and what is Sraffa's real role in developing the theory of value?

In his book, Sraffa considers the problems of value and price formation on the basis of schemes of simple and expanded reproduction structured in accordance with the principle of natural intersectoral connections between products. Consequently, *it is not value in its Marxist interpretation* but exchange proportions, exchange values that he analyses in the spirit of Ricardo's natural economics.

On the basis of the natural interrelationships of the intersectoral balance, a given volume of wages and a *single* rate of profit, he constructs a system of equations for deriving the prices of products (prices of production). This system of equations is used to analyse how prices will change under the influence of the changes in the distribution of the net product (rather, the so-called "surplus", i.e.

the excess of the product over the physical subsistence minimum) between profits and wages. Sraffa does not consider the causes of these changes, the factors which determine the shifts in the profit-wages ratio.

He shows that the effect of a rise (fall) in wages on the cost of producing various commodities depends on the proportion in which labour and capital are involved. The costs of the more labour-intensive goods will grow to a greater extent than the costs of less labour-intensive goods. If these goods are, for their part, inputs into the production of other goods, the change in the price of production of these other goods will depend on the share of the former in their costs, etc. As a result, the price of production could rise, but could also *relatively* fall, for there is no simple solution. If a given product is labour-intensive, but if its basic material inputs are capital-intensive, rise in wages will increase the labour inputs into the product concerned, but will relatively reduce the material inputs used in the manufacture of the given product. Thus, the price will be a resultant of these opposite forces.

From this it follows that it is impossible to find a commodity whose price of production would remain unchanged and would not depend on shifts in income distribution. In other words, the price of production cannot serve as a gauge of exchange proportions between goods.

Sraffa set out to find another measure of exchange value, a "physical" analogue of value which did not depend on changes in distribution and prices.

He asked this question: was it theoretically possible to construct an industry in which the relation of net product to the value of material inputs $\left(\frac{Y}{C}\right)$ did not change under the influence of changes in distribution and goals? He showed that such an industry could be brought out from the existing economy, and designated as a "standard industry".

To construct this "standard industry", he formulates the concept of "basic goods", i.e. goods which are, directly or indirectly, inputs into the production of all the other goods. It is the closed system of equations characterising the interrelationships between the production and consumption of these goods that constitutes the "standard industry". Its peculiarity is that both the natural structure of the product and the natural structure of the inputs in it are similar, so that, however prices may change, the $\frac{Y}{C}$ ratio remains constant. Sraffa and his followers regard the unit product in the "standard industry" as the "physical" measure of value which does not depend on price changes.

This theoretical system attracted close attention, especially among radical economists in the West, and became an issue of stormy debate.

Some claim, without any reservations, that Sraffa has been developing Marx's theory of value. That is the view taken by some radical US economists, like Sherman, who has written about the "Marx-Marshall-Sraffa theory of value".[1] This idea has been actively supported by British economists.[2]

But there is also the opposite view that Sraffa's theoretical works are not directly related to the Marxist theory of value, and that Sraffa has been developing the Ricardian and not the Marxist tradition in the theory of value, and has emphasised the fundamental distinction between the two.

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[1] E. K. Hunt and Howard Sherman, *op. cit.*, p. 41.

[2] In one of his works, Maurice Dobb said that the history of economic thought should be rewritten beginning from Jevons and the 1870 "marginalist revolution" just as it should be rewritten once again after Sraffa and the revolutionising discussions of the 1960s. Sraffa, Robinson and other critics of the theory of marginal productivity, Dobb said, were heirs to the "Ricardian-Marxist tradition" in analysing the problems of exchange and distribution. (Maurice Dobb, *Theories of Value and Distribution Since Adam Smith*, Cambridge University Press, London, 1973, p. 111.)

That is stressed, among others, by a group of economists (Suzanke de Bruenkoff, A. Medio, and others[1]), while P. Sweezy says in a review of Dobb's book that although Marx's theory did develop Ricardo's theory, it was at the same time its very opposite, because it contained a comprehensive critique of the capitalist mode of production. That is why it is fundamentally wrong to speak of a Ricardian-Marxist tradition, which Sraffa has allegedly developed. Sweezy adds:

> "The very title of the book of Sraffa, who, in Dobb's treatment, is the contemporary embodiment of the tradition ... is in sharp contrast to Marx's approach. Marx was emphatically not concerned with the 'production of commodities by means of commodities'. His subject was the production of commodities by means of human labour—and all that it implied for the civilisation and ultimate fate of the capitalist order."[2]

That is why there is a need for a more detailed comparison of Marx's theory of value and the theory which underlies Sraffa's analysis. First, the labour theory of value used by Sraffa, and Marx's theory of value are two different things. We believe that the failure to understand this, an effort to dismiss this important distinction or obscure it is the origin of the fundamental errors in assessing Sraffa's system. Indeed, the latter has adopted Ricardo's labour theory of value, which says that exchange proportions are based on labour inputs and that value is determined by labour time. That, Marx

[1] Suzanka de Bruenkoff, "Marx as a Ricardian". In: *Science and Society*, 1973, No. 2; A. Medio, "Profits and Surplus-Value: Appearance and Reality in Capitalist Production". In: *A Critique of Economic Theory*, ed. by E. K. Hunt and Jesse. G. Schwarts, Penguin Books, Harmondsworth, 1973, pp. 312-346.

[2] *The Journal of Economic Literature*, Vol. XII, June 1974, No. 2, p. 48

said, was the greatest scientific achievement of classical bourgeois political economy. But Ricardo failed to go beyond the purely quantitative consideration of the problem, beyond the concept of exchange value. Since he failed to bring out the category of abstract labour, he was unable to see the crucial distinction between exchange value and value as a crystallisation of this socially necessary abstract labour. Marx sharply criticised Ricardo for this incompleteness and the resultant confusion. He said that Ricardo

> "does not even examine the form of value—the particular form which labour assumes as the substance of value. He only examines the magnitudes of value, the quantities of this abstract, general and, in this form social, labour which engender differences in the *magnitudes of value* of commodities".[1]

The distinction which Marx drew between value and exchange value was of tremendous importance in understanding the distinctions in the movement of values and prices of production, surplus value and profit, and of the substance of the process which led to the evening out of the rate of profit and the transformation of value into the price of production.

Marx believed that the distinction between value and the costs of production was much more important than the movement of the costs of production under the impact of changes in wages, a question which Ricardo examined (and confused). Marx wrote:

> "He would also have seen how incomparably more important and decisive the understanding of this difference is for the whole theory, than his observations on the variation in

[1] Karl Marx, *Theories of Surplus-Value*, Part II, Progress Publishers, Moscow, 1975, p. 172.

cost-prices of commodities brought about by the rise or fall of wages."[1]

Marx proved that the very assumption of a general rate of profit could not be squared with a definition of value by labour time without an understanding of the two-fold nature of labour, and without a distinction between value and exchange value, surplus value and profit. He wrote:

> "Instead of *postulating* this *general rate of profit*, Ricardo should rather have examined in how far its existence is in fact consistent with the determination of value by labour-time, and he would have found that instead of being consistent with it, *prime facie*, it *contradicts* it, and that its existence would therefore have to be explained through a number of intermediary stages."[2]

Sraffa and his associates, in effect, analyse all the vulnerable aspects of Ricardo's theory of value which were so harshly criticised by Marx.

Like Ricardo, Sraffa does not recognise the two-fold nature of labour as embodied in commodities, or the special nature of the labour crystallised in value. According to Sraffa, value is only a definite measure of economic relations, but is not an expression of their substance. He regards value purely as a category of account, which can be obtained by reducing the prices of production to the inputs of labour, and nothing more. For him, value and price lie on the same plane of economic phenomena. Nor is it surprising that while Marx starts his analysis of price formation from the value structure of the product, Sraffa starts from its physical structure. These differences of approach spring from fundamental differences in methodology.

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[1] *Ibid.*, p. 176.
[2] *Ibid.*, p. 174.

Let us note that Sraffa himself does not claim anywhere to be a Marxist. He says that his theory is connected with Ricardo's, but not with Marx's. That is understandable, because his whole system is structured without the categories of analysis which are essential to Marxism: value as the embodiment of abstract social labour, the value of labour power, and surplus value.

From the standpoint of bourgeois economics, Sraffa's system marks a definite advance, a break with the vulgar subjectivist theory of value, and a development of the Ricardian tradition. But Sraffa does not rise to the summits of the Marxist theory of value, deliberately confining himself to the quantitative aspects of the problem.

Furthermore, Sraffa and his associates claim that an important advantage of the "standard industry" theory is the fact that it helps to establish a definite quantitative relation between the rate of profit and the distribution of the net product between profit and wages. If p is the rate of profit, and v the share of wages in the net product (Y), then the connection between p and v will be expressed in this formula: $p = \frac{Y}{C}(1 - v)$. The $\frac{Y}{C}$ ratio is the inverse of the capital-product coefficient. When the $\frac{Y}{C}$ ratio remains unchanged (this ratio is stable only in the "standard industry" and does not depend on price changes), the rate of profit will be determined exclusively by how the product is distributed between profit and wages. When the $\frac{Y}{C}$ ratio remains unchanged, the higher the v, the lower is the p, and vice versa, i.e. there is a stable inverse relation between the two.

Those who regard Sraffa's theory as a Marxist one assume that this "standard industry" equation provides excellent proof of the Marxist theory of exploitation, because it allegedly shows the existence of a direct connection between the rate of profit (p') and the rate of surplus value (m'), as expressed in the first part of the equation.

But Marx's theory of value does not at all imply such a rigid relation between profit and surplus value, and the possible relations between the two are analysed in Chapter Three of Volume Three of his *Capital*. He starts from a similar formula of the relation between the rate of profit (p) and the rate of surplus value (m):

$$p' = m' \frac{v}{K},$$

where $\frac{v}{K}$ is the value composition of capital. In order to prove his theory, he does not at all require the value composition to be constant. On the contrary, Marx emphasised that profit is a *form in which* surplus value is expressed, which cannot be brought out simply by mathematical calculations, but only through *analysis*.[1] He considers various cases when profit and surplus value may move in different directions owing to changes in the composition of capital. As a result, a rising rate of profit may correspond to a falling rate of exploitation, and vice versa. "The rate of profit," Marx writes, "depends on two main factors—the rate of surplus-value and the value-composition of capital."[2] Elaborating on this idea, Marx shows that the rate of profit also depends on the velocity of the capital turnover, on economies in the use of constant capital, on changes in the value of constant capital, etc.

The fundamental differences between Marx's theory of value and the one from which Sraffa starts determine the fundamental distinctions in the substance of the problem of the transformation of value into the price of production.

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[1] Karl Marx, *Capital*, Vol. III, Progress Publshers, Moscow, 1971, p. 48.

[2] *Ibid.*, p. 69.

The transformation problem is central to the Marxist theory of value, because through this process the value categories which express the substance of the capitalist mode of production are tied in with the actual categories which appear on the surface of economic reality: prices, profit, and wages. The law of value and the related laws of distribution are effected through the price-formation mechanism.

The establishment of this connection between theoretical and actual categories proves that the labour theory of value itself is correct and valid.

The transformation problem has a qualitative and a quantitative aspect (as, incidentally, do all the other theoretical problems considered by Marx) and is a unity of historical and logical analysis.

Marx concentrated on the qualitative content of the transformation problem. When analysing the mechanism of capitalist competition, and moving from abstract, inner categories to the concrete forms of their expression, he logically proved how value was transformed into the price of production. This is simultaneously the historical process in which the simple commodity economy is transformed into the capitalist economy.[1] Such an analysis also helps to bring out the social relations—the relations of exploitation—which lurk behind the simple relationship between commodities and prices. Herein lies the substance of the transformation

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[1] This problem was the subject of a discussion between Ronald L. Meek, on the one hand, and M. Morishima and G. Catephores, on the other. While the latter regard the transformation (of value into the price of production) problem as a purely logical process in which one logical category develops into another (see the relevant articles in *The Economic Journal* for June 1975 and June 1976), Meek regards the transformation of value into the price of production as a unity of the historical and the logical. (See: R. Meek, "Is There an 'Historical Transformation Problem?' A Comment." In: *The Economic Journal*, Vol. 86, June 1976, No. 342, pp. 342-347.)

problem and the ultimate proof for the theory of value itself.

Marx emphasised that an analysis of the transformation process does not amount to a mere establishment of some quantitative equation; it is an analysis of the transformation of substance into its form. He wrote:

> "Surplus-value and rate of surplus-value are, relatively, the invisible and unknown essence that wants investigating, while rate of profit and therefore the appearance of surplus-value in the form of profit are revealed on the surface of the phenomenon."[1]

But the transformation problem also has a quantitative aspect, which boils down to a demonstration of the idea that the sum-total of values is equal to the sum-total of the prices of production, and that the sum-total of surplus value determines the total profit which is distributed within the class of capitalists in accordance with the size of capital. Marx shows that this equation depends on the fact that the social price of production is regulated by the price of production of commodities produced with an average organic composition of capital, so that the fluctuations of values from the prices of production in industries with a higher or lower composition of capital are mutually cancelled out. It is this quantitative aspect of the transformation problem that was seized upon by Marx's critics, who ignored and sought to obscure its qualitative content.

The starting point for this criticism is the question of how changes in wages affect the prices of production and the relation between the prices of production and values. Let us note that Marx devotes a small chapter to this question (Chapter II) in Volume Three of his *Capital*, and says this about the importance he attaches to the problem of the

[1] Karl Marx, *Capital*, Vol. III, p. 43.

transformation of profit into average profit: "This is but a very secondary question compared with the other important points analysed in this part"[1]. Marx considers the influence of the changes in wages on the prices of production and shows that the latter influence relative prices but do not change the position of the industry with an average organic composition of capital as the regulating one, a fact which makes for the equality of the sum-total of values and the sum-total of the prices of production. This will be seen from the following numerical example.

1. Let the rate of surplus value = 100 per cent, and profit (p) = 20 units

Value	Price of Production
$70c + 30_v + 30_p = 130$	$70c + 30_v + 20_p = 120$
$80c + 20_v + 20_p = 120$	$80c + 20_v + 20_p = 120$
$90c + 10_v + 10_p = 110$	$90c + 10_v + 20_p = 120$
Total values 360 =	Total prices 360

II. Let us assume that wages have risen by 25 per cent

Value	Price of Production
$70c+37.5_v+22.5_p = 130$	$70c+37.5_v+15.4_p = 122.9$
$80c+25_v + 25_p = 120$	$80c+ 25_v+15_p = 120$
$90c+12.5_v+7.5_p = 100$	$90c+12.5_v+14.6_p=117.1$
Total values 360 =	Total prices 360

The changing relation between profit and wages in industries with an average composition of capital *does not change the value and price of production.*

We find that *if wages are raised:*

1) the price of production for a capital of average composition does not change;

2) the price of production for a capital of lower composition rises, but not in proportion to the rise in wages; and

[1] Karl Marx, *Capital*, Vol. III, p. 204.

3) the price of production for a capital of higher composition falls, but not in proportion to the rise in wages.

The fluctuations are cancelled out and the sum-total of prices continues to be equal to the sum-total of values.

> "Since the price of production of the commodities of the average capital remained the same, equal to the value of the product," Marx writes, "the sum of the prices of production of the products of all capitals remained the same as well, and equal to the sum total of the values produced by the aggregate capital. The increase on one side and the decrease on the other balance for the aggregate capital on the level of the average social capital"[1].

But assuming that the changes in prices influence not only wages but also the amount of constant capital in the industry that regulates price formation, the picture becomes less obvious and requires some corrections. Marx also noticed this and wrote:

> "Should the rise or fall in wages be due to a change in the value of the necessities of life, a modification of the foregoing findings can take place only to the extent that commodities, whose change of price raises or lowers the variable capital, also go into the constant capital as constituent elements and therefore affect more than just the wages alone. But if they affect only wages, the above analysis contains all that needs to be said"[2].

Indeed, assuming that price changes affect not only wages, but also the amount of constant capital in the industry that regulates price formation, the picture becomes less obvious.

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[1] *Ibid.*, pp. 201-202.
[2] *Ibid.*, pp. 203-204.

Let us see what happens if we assume that in the average-composition industry the value of capital has also risen by 25 per cent. Then surplus value = 100. The price of production in this industry goes up, and the industry ceases to be the regulating one. The quantitative relation between prices and value becomes indefinite, and there is a need for some additional research to discover it. But Marx did not consider this issue to be sufficiently important for his theory, and left it open.

Thus, the quantitative aspect of the transformation problem does indeed call for additional study; Sraffa's system of standard industries may be seen as a particular solution of the problem.[1] However, this quantitative aspect is far from playing any definitive role in the Marxist theory of value. It is a particular question, and Sraffa's line of argu-

[1] In this context, Meek says: "Sraffa is postulating precisely the same relation between the average rate of profits *and the conditions of production in his 'standard' industry* as Marx was postulating between the average rate of profits *and the conditions of production in his industry of 'average organic composition of capital'*. What both economists are trying to show, in effect, is that (when wages are given) the average rate of profits, and therefore the deviations of price ratios from embodied labour ratios, are governed by the ratio of direct to indirect labour in the industry whose conditions of production represent a sort of 'average' of those prevailing over the economy as a whole. Marx reached this result by postulating as his 'average' industry one whose 'organic composition of capital' was equal to the 'social average'. But his result could only be a provisional and approximate one, since in reaching it he had abstracted from the effect which a change in the wage would have on the prices of the means of production employed in the 'average' industry. Sraffa shows that the same result can be achieved, without abstracting from this effect at all, if we substitute his 'standard' industry for Marx's industry of 'average organic composition of capital'. Sraffa's 'standard' industry, seen from this point of view, is essentially an attempt to *define* 'average conditions of production' in such a way as to achieve the identical result for which Marx was seeking". (R. Meek, "Piero Sraffa's Rehabilitation of Classical Economics". In: *Science and Society*, Spring 1961, Vol. XXV, No. 2, pp. 155-156).

ment has an important positive significance only because the question has been so inflated by bourgeois economists and has had a big part to play in anti-Marxism. But it would be an extreme exaggeration to regard it as a further development of the theory and as a solution of the transformation problem in the true Marxist sense.

Summing up what has been said, one could draw the conclusion that Sraffa's system can be used for solving a fairly particular aspect of the transformation problem, but his analysis cannot in any sense be identified with Marx's much broader approach. Nor is this accidental, because, as it has been shown above, Sraffa takes the Ricardian approach, and shuns Marx's view of value as an embodiment of social relations. He also shuns the very concept of transformation as a process of conversion—through the appropriate economic mechanism—of the inner categories and laws of capitalist production into the forms of their expression.

The fundamental difference between Marx's theory of value and mechanism of transformation of value into the price of production from Sraffa's theory stands out most clearly when we turn to a comparison of the categories of distribution. Let us emphasise that Sraffa's system does not include any theory of distribution at all (which is why we feel that the suggestions that Sraffa's theory provides the starting point for a new theory of distribution are groundless). Like Ricardo, he assumes the same rate of profit as something established from outside. Its level is also determined by forces that are outside the framework of his system of techno-economic ties.

The same applies to wages. Refusing to recognise the category of the value of labour power, Sraffa sets a limit for wages, namely, the physically necessary minimum means of subsistence, so that everything over and above this is the result of a sharing out of the so-called "surplus" between profit and wages. He has no objective basis or uniformities governing this sharing out, and this is incidentally emphasised by John Eatwell, an economist who has vigorously advocated Sraffa's theory. He admits that Sraffa has no objective basis for determining the level of wages and distributing the net income.

> "The apportionment of output is therefore an open element in the analysis of price formation, and the system may only be closed by the addition of a new theory to determine the real wage or the rate of profit. Sraffa leaves the issue open", says Eatwell. "He develops the analysis in terms of the possible wage-profit-rate configurations for the given system of production and the given composition and scale of output."[1]

Let us note that many of those in the West who take part in the discussion of Sraffa's theory of value have also noted the fundamental distinction between the Marxist view of the transformation problem and Sraffa's.

In an article on the transformation problem, the well-known US economist William J. Baumol wrote:

> "One must also reject the assertion that Marx thought prices had to be *deduced* from values via his transformation calculation... Prices and values are, in short, not the same thing. Values are not approximations to prices nor a necessary step in their calculation. Rather, one is a surface manifestation, while the latter is intended to reveal an underlying reality... The point of the value theory may then be summed up as follows: goods are indeed produced by labour and natural re-

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[1] J. Eatwell, "The Irrelevance of Returns to Scale in Sraffa's Analysis". In: *The Journal of Economic Literature*, March 1977, Vol. XV, No. 1, p. 64.

sources together. But the relevant social source of production is labour... The competitive process that appears to show that land is the source of rent and capital the source of profits and interest, is merely a distributive phenomenon and conceals the fact that labour is the only socially relevant source of output. This is the significance of the value theory and the transformation analysis to Marx"[1].

We could continue the confrontation of views of Sraffa's work, because it did generate a great discussion and is of much interest in itself. Let us note merely that the discussion is still going on, and its emergence with the publication of the works of Joan Robinson and Sraffa sharply criticising the neoclassical postulates of bourgeois political economy is an extremely remarkable phenomenon. The two economists have done much for the criticism of the neoclassical theory of value and distribution, at one time the chief antagonist of the Marxist theory of value and exploitation.

Sraffa revived the Ricardian approach and returned to the labour theory of value, although he stopped short of adopting its Marxist interpretation. Interest attaches to his elaboration of the qualitative aspects of the formation and change of the prices of production and also his solution of the transformation problem.

However, we do not share the delights of Sraffa's admirers who hold his work to be the latest word in the development of Marxism. The analysis shows that Sraffa departs from the Marxist interpretation of the crucial categories of the political economy of capitalism—value, surplus value, the value of labour power, and others—without which Marxism loses its real substance.

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[1] W. J. Baumol, "The Transformation of Values: What Marx 'Really' Meant (An Interpretation)". In: *The Journal of Economic Literature*, Vol. XII, March 1974, No. 1, pp. 55, 59.

3. Post-Keynesian Models of Growth and Distribution

How have the critics of marginalism countered the neoclassical theory of growth and distribution?

They have come up with an alternative: the post-Keynesian theory of growth and distribution, whose fundamentals were laid by the works of Joan Robinson and N. Kaldor, and further elaborated by L. Pasinetti, J. Kregel and other economists. This theory is based on two assumptions.

1. The rate of growth depends on the distribution of income, because total savings are the sum-total of savings from wages and from profits. But because receivers of wages and of profits have a different propensity to save, changes in distribution will change the total savings.

2. The distribution of income itself depends on the rate of accumulation of capital, which determines the rate of profit, and consequently the share of profit in the income. The share of wages and the wage fund is determined as a residual magnitude.

This brings out the distinctions from neoclassical theory: there are no categories of marginal products, which determine the rate of profit and the basic wage. The rate of growth is determined not just by the availability of resources and the pace of technical progress, but by the intensity of accumulation and the propensity to save.

Let us first consider Kaldor's model.[1] In it, the rate of growth and income distribution are internally interrelated categories. Considering that the income of society, as Kaldor assumes, is distributed between the various classes, each of which has its own (constant) propensity to save, this relation in distribution determines the level of savings in society as a whole, and consequently, the rate of

[1] See: N. Kaldor, "Alternative Theories of Distribution". In: *The Review of Economic Studies*, 1955-1956, Vol. XXIII (2), No. 61.

accumulation and the rate of growth. On the other hand, the attainment of a given rate of growth requires a given rate of accumulation, and consequently a corresponding distribution of income. The rate of growth and the rate of accumulation are, therefore, factors which, for their part, affect the distribution of the national income. This interrelationship is illustrated by the following system of equations:

$$Y = P + W, \ \dot{I} \equiv S, \ S \equiv S_W + S_P, \ S_W = s_W W, \ S_P = s_P P,$$

$$\dot{I} = s_P P + s_W W = s_P P + s_W (Y - P) = (s_P - s_W) P + s_W Y.$$

Hence

$$\frac{\dot{I}}{Y} = (s_P - s_W) \frac{P}{Y} + s_W, \tag{1}$$

$$\frac{P}{Y} = \frac{1}{s_P - s_W} \cdot \frac{\dot{I}}{Y} - \frac{s_W}{s_P - s_W}, \tag{2}$$

where Y is the national income; W the income of labour (wage fund); P the income from property (profit); $\dot{I}$ investment; S savings; S_W the total savings from wages; S_P the total savings from profit; s_W the share of savings from wages; s_P the share of savings from profit.

In Kaldor's equations, the distribution of income and the rate of accumulation are rigidly connected with each other. When s_P and s_W are given, the share of profit in the national income (P/Y) is determined exclusively by the rate of accumulation ($\dot{I}/Y$), and the rate of accumulation depends on the share of profit in the national income. Kaldor uses this interrelationship for interpreting two basic problems in the theory of growth: the problem of economic equilibrium, and the factors which determine the rate of long-term growth.

On the equilibrium problem, Kaldor assumes that the introduction of the mechanism of distribution into the model (provided $s_P > s_W$) makes the system more stable and more capable of automatically restoring the equilibrium. In this sense, his growth model differs substantially from Harrod's model. Kaldor believes that any change of $\dot{I}$ with respect to S (something that in Harrod's model produces cumulative processes of decline in production or its growth) sets in motion the mechanism of income redistribution, which adapts S to the new level of $\dot{I}$.

In this redistribution of incomes, inflationary processes have an important part to play. Kaldor assumes that an increase in investment and a general growth of demand under full employment will induce prices to rise faster than wages. The distribution of income will change in favour of profit, and the share of the working class will decline. Because savings from profit are higher than from wages, savings will tend to grow. The equality of S and $\dot{I}$ will be restored. Conversely, if investment is reduced and total demand falls, prices tend to fall faster than money wages, distribution changes in favour of the workers, savings go down, and the equality of S and $\dot{I}$ is also restored. (In Western economic writings, this mechanism has been designated as the "Kaldor effect").

The distribution of income has a crucial role to play also in the analysis of long-term growth factors. It follows from the equations given above that if s_P and s_W are constant, an increase in the rate of accumulation and, consequently, in the rate of growth requires an increase in the share of profit in income (P/Y), while any fall in the rate of accumulation will entail a fall in the rate of profit. So, the rate of accumulation is a key factor which determines the long-term trends in the distribution of the national income.

Kaldor's model includes the essential techno-economic relationships which in certain conditions take shape between accumulation, growth, and distribution. At the same time, one should neither lose sight of the rigid premises on which the model is based and which far from always correspond to the actual state of things.

Thus, for instance, the restoration of a short-term equilibrium on the basis of the "Kaldor effect" described above, implies that there is a greater change of prices than of wages: in a favourable market outlook, they change faster than wages, and in a period of recession they fall faster (or rise slower) than wages.

But this notion about the dynamics of prices and wages is not backed by facts and can only be accidental. The dynamics in the relationship between prices and wages described by Kaldor may not occur at all under monopoly domination and the general inflationary growth of prices, and also the struggle carried on by the trade unions to uphold the gains of the working class and maintain the growth of real wages. That is why the notion that the mechanism of economic adaptation can be modified by a change in the distribution of incomes is an abstraction which does not accord with reality.

Kaldor's model also suggests that long-term growth rates can be increased merely through a redistribution of the national income in favour of profit and an increase in the rate of accumulation. Such conclusions are used to justify the reactionary policy of the monopolies and the bourgeois state, which are forced to curb the working people's vital interests allegedly for the sake of economic growth.

Actually, faster growth rates dictate the need for an increase in the rate of accumulation only if capital intensity is constant or growing. However, statistical studies show that in some periods faster growth rates can be achieved even with a declining capital intensity through greater efficiency of capital inputs, which reduces the need for accumulation.

The vast non-productive expenditures which now burden capitalist society, especially government military spending, are also completely ignored in Kaldor's abstract model. Introduction into the model of the magnitude of government revenues with a corresponding "propensity to save" could open up another source of growth and increase in the rate of accumulation besides the working people's incomes.

Finally, the premise concerning the invariable shares of saved income—s_P and s_W—is excessively rigid. Empirical studies of this problem show that these shares tend to change depending on the growth of incomes and many other factors.

Kaldor seeks to discover the main reasons for the stability of the distribution of the national income since the end of 19th century.[1] He looks for these in the purely techno-economic uniformities of growth. In order to simplify his reasoning, he assumes that the share of savings from wages is equal to zero ($s_W = 0$). Then equation (2) assumes the form

$$\frac{P}{Y} = 1/s_P \frac{\dot{I}}{Y}.$$

According to Harrod's formula, the rate of accumulation ($\dot{I}/Y$) is determined by the rate of growth and the coefficient of capital intensity ($s/YC_r g$). Hence

$$\frac{P}{Y} = \frac{1}{S_P} C_r g.$$

According to this formula, the share of profit in income is determined by the share of savings from profit (s_P), the rate of growth (g) and the "capital-

[1] "In fact no hypothesis as regards the forces determining distributive shares could be intellectually satisfying unless it succeeds in accounting for the relative stability of these shares in the advanced capitalist economies over the last 100 years or so, despite the phenomenal changes in the techniques of production, in the accumulation of capital relative to labour and in real income per head. (N. Kaldor, "Alternative Theories of Distribution". In: *The Review of Economic Studies*, 1955-1956, Vol. XXIII(2), No. 61, p. 84.)

product" coefficient (C_r). If the first two indicators remain constant, the stability of the share of profit in income will be determined by the stability of the capital coefficient.

In order to explain and substantiate this stability, Kaldor introduces the category of "technical progress function", whose essence is that technical progress in itself is never either capital-intensive or capital-saving. The dynamics of capital intensity depends on the use of the existing technological potentialities. Optimal use of technological potentialities, which the economic system seeks to achieve, is always characterised by the equality of increment of capital and product, and therefore by a trend towards the stability of the capital coefficient.[1]

The increment of the product will be smaller than the increment of capital when the technological potentialities are not being fully utilised. In these conditions, incentives appear for increasing the rate of accumulation leading to full use of the technological potentialities, a higher rate of product increment and stabilisation of the "capital-product" coefficient.

On this basis, Kaldor puts forward the concept of two stages in the development of capitalism. Many of its propositions are doubtful, like the approach to the relation between capital accumulation and the use of technological potentialities at various stages of the development of capitalism. It is also hard to accept the idea that in the 19th century only the scale of capital accumulation blocked the use of technological potentialities in a way that would ensure equality of the increment of product and capital. Technological potentialities are not something that is external and that develops independently of the level of economic development. The growth of capital intensity in the 19th century,

[1] See: N. Kaldor, "A Model of Economic Growth". In: *The Economic Journal*, No. 268, December 1957, Vol. LXVII, pp. 591-624.

which continued until the 1920s, resulted from an in-depth structural remodelling of the capitalist economy and its industrialisation, and developed alongside the materialisation (on the basis of capital accumulation) of the outstanding technical advances of the day.

The slow-down and stabilisation of the dynamics of capital intensity in the 20th century are based on deep-going changes in the very nature of technical progress, which helps tremendously to enhance the efficiency of material inputs, the growth of the output-capital ratio and of labour productivity.

Although Kaldor does remark on the excessively generalised character of his concept, one has to note that its shortcoming does not consist in excessive generality, but in the fact that Kaldor seeks to fit into the rigid framework of purely technological changes the whole complexity of the socio-economic relations which characterised the growth of free-competition capitalism into monopoly and state-monopoly capitalism, and which affected the nature of distribution.

What are the new elements that Joan Robinson introduced into the analysis of this problem? She considers the interrelationship between distribution and economic growth in a much broader plane. While Kaldor connects the distributive proportions above all with the amount of accumulation, Robinson also regards them as a factor determining the scale of effective demand, and consequently, a condition for realising the social product.[1]

Her model is based on the following premises:

—the economy has two sectors turning out capital goods and consumer goods;

—the techniques of production are given, so that the technological coefficients are fixed;

[1] See: J. Robinson, *The Accumulation of Capital*, Macmillan & Co. Ltd., London, 1956, p. 100.

—investment is the basis and motive force of capitalist production, so that the rate of investment ($\dot{I}/Y$) is the most important external variable.

Robinson's assumption is that the value of the end product in each division is made up of wages (W) and a so-called quasi-rent consisting of profit and depreciation (Q).

$$W_1 + Q_1 = Y_1; \quad W_2 + Q_2 = Y_2.$$

Between these two equations (if there is simple reproduction, i.e. if all the wages are consumed, and the profit is invested) the following relationships are established:

$$W_1 + W_2 = Y_2$$

$$W_1 = Q_2, \quad Q_1 + Q_2 = Y_1.$$

How are these relationships established? If the $\dot{I}/Y$ ratio is given, then, with the given techniques of production, it will determine the distribution of labour between the two sectors of social production, i.e. W_1/W_2. Since W_1 has been determined, then, under the given labour productivity, the magnitude Y_1 has also been determined, and consequently, Q_1 as well (since $W_1 + Q_1 = Y_1$). Furthermore, W_1 will determine the magnitude Q_2. But the relation between them, expressed in prices, will be such as to ensure a rate of profit in Sector II that is not lower than that in Sector I. Consequently this equation, together with the rate of profit in Sector I, will also determine the price formation.

As a result, $Q_1 + Q_2 = Y_1$.

If we deduct depreciation from the left side of this equation, and compensation from the right side, we shall obtain the total profit on the left side, and net accumulation on the right side.

$$P + P_1 + P_2 = \Delta K.$$

Dividing the whole by K, we obtain $P/K = \Delta K/K$, i.e. the rate of profit is equal to the rate of capital accumulation. From this the author draws the cardinal conclusion stated above: the rate of capital accumulation determines the rate of profit. The larger the accumulation, the higher the profit; the returns are proportional to the investment.

Consumption from profit and savings from wages will modify this equation somewhat. Consumption from profit will increase demand, raise prices and lead to a situation in which the rate of profit will be higher than the rate of accumulation $[(P/K) > (\Delta K/K)]$. Conversely, savings from wages will reduce demand, prices will decline, the rate of profit will fall and will be lower than the rate of accumulation $[(P/K) < (\Delta K/K)]$.

In this way, Robinson proves that the rate of profit is determined by the rate of capital accumulation and the propensity to save. Investments, with the businessman's social mentality as the motive force, is the crucial variable of the system.

Robinson believes that the rate of capital accumulation cannot be random, for there is an optimal level of accumulation rate ensuring a distribution of the national income under which the growth of effective demand advances in step with the growth of production. Too high a rate of accumulation makes for an excessively high share of profit in income and reduces the share of the working class. This produces an "inflationary barrier", i.e. inflationary processes develop in consequence of which falling living standards induce the workers to fight for higher money wages in order to maintain their habitual living standards. Too low a rate of accumulation leads to a fall in the rate of profit and of its share in income, thereby reducing the incentives for economic growth. Tendencies to stagnation appear in the economy.

But tendencies to stagnation may also emerge under an excessive rate of profit, where the profit results from monopoly and not from an excessively high rate of accumulation.

Because Robinson takes the left-wing view of Keynesian theory with its reformist illusions of some "progressive capitalism", she assumes that tendencies to stagnation can be prevented through the trade union struggle of the working class.[1]

Robinson believes that a rise in wages (to the extent of growing labour productivity) not only resolves the contradictions in the realisation of capitalist growth under technical progress, but is also its most important stimulus.

Her view is that society always has a definite range of technological solutions for this or that technical problem which is determined by the level of labour productivity and the capital per worker ratio: as a rule, the technology which ensures a higher level of labour productivity requires larger inputs of capital per unit of labour, so that it is the level and dynamics of wages that determine the limits within which technology is profitable. The higher the wages, the more profitable it is to use less labour-intensive and more capital-intensive technology.

Robinson emphasises that under competition it is the rise in wages that determines the growth of productivity, and not vice versa.[2]

The suggestion that higher wages are a condition for realising the product and an incentive to technical progress is a progressive one because it meets

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[1] "The main defence against the tendency to stagnation comes from pressure by trade unions to raise money-wage rates... If by this means real wages can be made to rise as fast as output per man the root of the trouble is cut, and the economy can accumulate capital and increase total product at the rate appropriate to the pace at which technical improvements are being introduced, just as though competition were still active". (J. Robinson, *op. cit.*, p. 94).

[2] "It might be possible to have higher wages without higher productivity (provided that there was a lower rate of accumulation), but it would not be possible (under competitive conditions) to have higher productivity without higher wages... A low degree of mechanisation is a symptom of the underlying cause of low real wages, not a cause of low wages in itself". (J. Robinson, *op. cit.*, pp. 130, 131.)

the economic interests of the working class engaged in a determined struggle to improve its living standards.

We believe, however, that her theoretical reasoning is based on erroneous premises.

First, she assumes that higher wages can paralyse the contradictions of capitalist reproduction, which spring from the tendency to monopolisation. But the contradiction between production and consumption is intrinsic to the capitalist mode of production. There is no doubt that the monopoly practice of raising prices does, of course, sharpen this contradiction, but it is a contradiction that is always present under capitalism, whether under free competition or monopoly. It is an expression of the basic contradiction of capitalism, the contradiction between the social nature of production and the private form of appropriation. Working-class consumption under capitalism is not determined simply by the play of market forces, as Joan Robinson suggests, but by the value of labour power, and this creates very limited potentialities for a growth of popular consumption under capitalism. Wages, as any other prices, may deviate from value, may be higher or lower than the latter, but they cannot cut free from their value basis without jeopardising profits, the basic incentive to capitalist production.

The workers' economic struggle undoubtedly plays an important rôle in defending the working people's living standards against encroachments by capital, but its importance should not be overrated. It can help the workers to maintain or somewhat improve the living standards they have achieved, but this struggle cannot in itself eliminate the laws of capitalist production or the conditions of the exploitation of the working class. At definite historical stages in some countries, this struggle can help the working class in one period or another somewhat to ease the contradiction between production and consumption, but it is impossible to do away with this contradiction without abolishing capitalism itself.

Second, the superficial view of the contradictions of capitalism taken by Joan Robinson and some of her associates is the source of their utopian illusions that "enlightened" monopolists, allegedly realising the need to "live and let live", could or have already begun to pursue a deliberate policy of raising wages. Thus, she believes that it is possible to set up a society in which "progressive" monopolists and trade unions could collaborate, because both have an equal stake in higher wages: the former, because this creates demand and stimulates technical progress; and the latter, because it improves their living standards.

Meanwhile, the facts are that programmes for voluntary cooperation between workers and "progressive" employers are hopelessly out of touch with the realities of capitalist society, its class contradictions, and the working-class struggle for a radical transformation of capitalism. The capitalists and the monopolies have never willingly limited their profits and will never do so of their own accord, because this runs counter to the very nature of capitalism, whose mainspring is surplus value and profit, its converted form. The long historical record shows that growing wages result from ceaseless and determined struggle by the working class, its unity and resolve to stand up for its vital interests, and never result from the employers' "consciousness" or good will.

Post-Keynesians (Joan Robinson, in particular) frequently emphasise that their theory of distribution is akin to Marx's analysis of reproduction. One could be left with such an impression if one were to analyse, for instance, Joan Robinson's schemes of reproduction. She seeks to derive all the basic interrelationships of growth and distribution on the basis of techno-economic interrelationships arising in production and exchange between the two departments of social production, production of capital goods and consumer goods.

However, her schemes do not contain the main elements of Marx's analysis, namely, the interrelationship between the physical and the value structures of the product. Joan Robinson, like her followers, seeks to do away both with the value structure and with value categories altogether. She does not take the value of labour power as the inner regulator of wages. Instead, she has an "inflationary barrier", i.e. a low level of wages resulting from excessive rates of accumulation, which force the workers to reduce these through a struggle for higher money wages.

Consequently, her analysis runs in a different plane, for Marx starts from the form in which phenomena appear and goes on to show their substance, from prices to value, from wages to the value of labour power, from profit to surplus value, and so unravels the secrets of capitalist exploitation.

The real importance of the post-Keynesian theory of distribution consists in the fact that it is an attempt to tie in the proportions of distribution with the main proportions of reproduction, something that helps to broaden the view of the macroeconomic mechanism of economic growth. But the socio-economic conclusions which have been drawn from it fall short of the true scientific interpretation of the nature of the capitalist mode of production and distribution.

4. Theory of Economic Growth and the Realities

A look at the development of the theory of economic growth gives a better understanding of the causes behind its present state of crisis.

The main group of causes lies in the fact that both the Keynesian and the subsequent neoclassical theories of growth can no longer yield anything that is substantially new either for the advocacy of capitalist reproduction or for a better understanding of its mechanism (because of their methodological premises, the range of economic phenomena they consider, and the methods of analysis). There are various indications that their inner potentialities have been worked out.

On the one hand, there is an endless structuring of ever more refined models claiming to give an ever subtler understanding of individual and particular processes and phenomena in economic growth with ever fewer possibilities of verification, which makes these models of little use in practice and converts them into an exercise in "art for arts' sake". With the introduction of additional corrections in the mode of expression of capital, the nature of technical progress, and the behaviour of individual economic magnitudes, these models became ever more complexified and refined. The mathematical refinements, however, frequently meant a further departure from the statistical basis which should have been used to fill these models with a real and viable content, without which they are dead. Besides (and this is the main thing), the introduction of all manner of additional corrections did not affect the cardinal premises of neoclassical theory (namely, the premises of free competition, equality of the marginal products to the prices of production factors, absence of the problem of realisation, etc.), and altogether failed to reflect the specific features of monopoly capitalism.[1]

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[1] That was the point made by Wassily Leontief, who emphasised with alarm the growing gap between economic theory, clothed in effective mathematical forms and the meagre statistical basis with which it is increasingly losing touch and which "clearly cannot support the proliferating superstructure of pure, or should I say, speculative economic theory" (W. Leontief, "Theoretical Assumptions and Nonobserved Facts". In: *The American Economic Review*, March 1971, Vol. LXI, No. 1, p. 1).

On the other hand, these models, operating with a narrow range of factors—labour, capital, technical progress—are abstracted from the key exogenic factors, and this frequently distorts the conclusions that could be drawn on the basis of these factors.[1]

Having failed to fulfil its main purpose—to become the theoretical basis for state-monopoly regulation—the modern theory of growth has also failed to cope with its ideological task of providing a basis for the apologetics of state-monopoly capitalism.

That is why many bourgeois economists, seeing no point in further abstract theoretical modelling, have been moving into the field of more concrete analysis of individual economic-growth factors.

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[1] In this context, G.D.N. Worswick criticised the general state of economic science and remarked: "Consider as a first example the theory of economic growth, which has taken the form of the elaboration of a great variety of economic models whose behaviour is examined and whose performance is contrasted with that of other models. There is no question but that these models throw up fascinating problems, taxing one's intellectual powers to the full, but there is very little of it which is of any help in answering such questions as why growth rates differ among countries and between periods. 'Given the assumptions common to the models (no government, no international trade and so on), this is not surprising, and it may reasonably be argued that most model-builders have not been trying to do this anyway'. (F. H. Hahn and R.C.O. Mattews, "The Theory of Economic Growth: A Survey". In: *The Economic Journal*, December 1964)" (G. D.N. Worswick, "Is Progress in Economic Science Possible?" In: *The Economic Journal*, March 1972, No. 325, Vol. 82, p. 77).

Ronald Britto, the author of a survey of recent developments in the theory of economic growth, wrote: "Much scepticism has been expressed about the ability of such models to explain developments in the real world, a scepticism that has been probably shared by the model-builders themselves." He quotes Solow saying: "I don't think that models like this lead directly to prescription for policy or even to detailed diagnosis... They are more like reconnaissance exercises." (R. Britto, "Some Recent Developments in the Theory of Economic Growth: An Interpretation". In: *The Journal of Economic Literature*, December 1973, Vol. XI, No. 4, p. 1344).

This is expressed, in particular, in the switch to a more detailed analysis of the problems of scientific and technical progress, which, according to various calculations, accounts in the United States, for instance, for over one-half of the rate of national income growth. Hence the emergence of some new lines of bourgeois economics, which have obviously branched off from the theory of economic growth, like the "economics of scientific and technical progress", the "economics of education", the theory of "human capital", and so on.

The sharp criticism of the methodological principles of neoclassical theory by bourgeois economists of various persuasions is a clear indication of the crisis of economic-growth theory, especially of its neoclassical version.

Above we showed the role of the Cambridge School, whose members have made a contribution to the logical overthrow of some fundamental premises of the neoclassical theory of production and distribution.

In addition to this group, neoclassical theory is being attacked by John Kenneth Galbraith, the leader of contemporary institutionalism and bourgeois reformism. Neoclassical theory is also being sharply criticised by the French "social" school of political economy.

The works of all these economists and their criticism of the formal-logic principles of neoclassical theory have a strong influence on radical political economy and on young academics.

The theory of economic growth has also proved to be unfit for practical use. The assumption of traditional theory was that the attainment of high rates of increment (of the national income) automatically leads to a rise in the living standards of all the sections of the population, and ensures the necessary international positions in the competitive struggle between the capitalist countries and in the competition between the two systems. That is why attention was mainly focussed on a narrow group of techno-economic factors which determine the rates of growth, and on the conditions for sustained growth.

Experience showed, however, that the assumptions of that theory were a far cry from reality.

It turned out, in fact, that rapid economic growth fails to eliminate unemployment even in the period of cyclical upswing, because structural factors come to play an ever greater role in the dynamics of unemployment. Unemployment is increasingly connected with inadequate standards of education and skills among some sections of the population, because of the system of education and training of manpower and the inadequate appropriations made for these purposes by the capitalist governments. This problem tends to be further aggravated in time of recession. Thus, it was mostly the low-skilled or unskilled workers who lost their jobs during the general economic recession in the United States in 1974-75, when unemployment rose to 8 per cent.

Experience showed that rapid national income growth did not at all entail a corresponding improvement in the well-being of the whole population, as bourgeois propaganda has claimed. It is true that real wages and consumption of material goods tended to increase, but the run-away inflation in the 1970s markedly slowed down that growth, and from 1973 to 1975 led to a drop in real wages in most developed capitalist countries. Inflation has become a devastating force defying control by the capitalist governments. In order to curb inflation, they have to sacrifice the goals of economic growth. Conversely, stimulation of economic growth increases the risk of even faster inflation.

Experience has shown that economic growth does not mean any reduction in social inequality. Add to this the fact that rapid economic growth under uncontrolled monopoly operation increasingly clashes with the requirements of man's harmonious interaction with the environment, so worsening many indicators of the "quality of life" which are vitally necessary for man's existence. There is the disastrous pollution of water, air and space, the rise in urban noise level, and the disappearance of forests and green fields. All of this commands a new approach to evaluating the necessary rates of growth, to the problem of its government regulation, and a switch of attention to its negative effects.

The problem of growth rates is also compounded by the emergent shortage of various economic resources and their growing cost. This applies especially to the capitalist countries' energy industry, which is in a state of profound crisis.

The shortage of some key resources, the high rates of inflation, and the general growth of the costs of economic growth engender long-term tendencies towards a slowing down of growth rates in the capitalist economy. The first signs of this slowdown appeared during the 1974-75 economic crisis which hit most of the developed capitalist countries.

All of this shows that far from toning down, high growth rates increasingly sharpen the contradictions intrinsic to capitalism.

However, the traditional bourgeois theory of economic growth proved to be out of touch with these burning problems in the development of contemporary capitalism. This largely predetermined its crisis, the criticism of its principles and conclusions among bourgeois economists themselves, and the quest for new and broader concepts of capitalist economic development.

Economic-growth policy is also faced with new problems. Traditional theory formulated two basic lines of state-monopoly regulation of economic growth:

a) short-term regulation of the economy to flatten out cyclical fluctuations and attain sustained growth. Here, the Keynesian concept relied on a fairly broad system of measures in credit, monetary and fiscal policy, and also on the manipulation of government spending to regulate effective demand. Neoclassical theory, in its latest form of monetarism, advocated only the principle of government intervention in the economy—the maintenance of a stable growth of money supply—assuming that in these conditions the automatic forces of adaptation would ensure sustained growth of the capitalist economy without outside help;

b) the maintenance and development of the economic potential for the purposes of increasing growth rates over a long term through an influence on the basic growth factors, on technical progress in the first place.

Both lines of this economic policy ran into insuperable difficulties as the contradictions of capitalism were sharply aggravated.

The rapid development of inflation in the longest postwar economic crisis of 1974-75, and the new factors (as a rule relating to costs and not to demand) which fuelled inflation, made it extremely difficult to pursue a policy of stabilisation by means of the traditional regulation of effective demand. The Keynesian anti-cyclical set of instruments proved to be ineffective. But in these conditions, the monetarists' proposals appear to be even more utopian.

The policy of sustained economic growth, oriented mainly upon factors which increase growth rates (technical progress and the related investments into research, education, the production infrastructure, etc.) also proved to be extremely one-sided in these conditions. Although these lines of economic growth are still important, other aspects of economic growth begin increasingly to come to the fore.

Instead of the orientation upon a boundless increase of potential growth rates, the question of "rational" limits both for the growth of production and consumption of material goods is an ever more pressing issue. The scarcity of some raw material resources, the energy crisis, the growing cost of raw material and energy resources, and the worsening of many indicators of the quality of life make it necessary to think about the growth rate on which sustained-growth policy should be oriented. This is a question that has up to now been beyond the ken of traditional theory.

If the conditions for economic growth are to be ensured, there is also a need for new forms of government intervention in the economy, a reorientation of resources towards the development of some spheres of the non-production infrastructure, and a general increase in government spending. But this inevitably produces fresh contradictions relating to the sources of government spending and a further development of inflationary processes.

All of this shows that the theory of economic growth is at a crossroads. The old notions have been depreciated. The need has arisen for a much broader concept of growth that would not only provide a new approach to the advocacy of capitalism but also pave the way for new forms of long-term economic regulation with an eye to the changing conditions and criteria of economic development.

However, the hopes for a substantial "renewal" of bourgeois economics are illusory. Such a "renewal" is ultimately determined by the social command of the monopoly bourgeoisie, for which the "scientific" analysis of capitalist reproduction is confined to the narrow framework of a quest for new possibilities of an essentially class "regulation", or, at most, some reform of the capitalist economy.

CHAPTER THREE

THE "STABILITY" PROBLEM: MONETARISM VS. KEYNESIANISM

The question of the degree and limits of the "internal stability" of the capitalist economy (in other words, of the capacity of the economic mechanism to overcome automatically and with adequate speed, without government interference, the disruptions in the process of reproduction) has long been broadly debated in economic writings. The answer ultimately determines the recommendations for state-monopoly intervention in economic life. Polemics in this field usually flare up in periods when the economic and social contradictions of capitalism are sharpened, so plunging into crisis all the old economic doctrines and conceptions.

The idea that the capitalist economy is "basically stable" and "internally coordinated" underpinned the neoclassical theory of general equilibrium, which took shape in the late 19th century and prevailed up until the 1930s. Under the influence of the unprecedented crisis of 1929-33, Keynes criticised this theory and proposed a new view of the reproduction mechanism.

In the postwar period, Western economists came out with serious and extensive opposition to Keynesian theory, especially to its thesis concerning the "internal instability" of capitalism. They also criticised the Keynesian recipes for economic regulation, the use of which eventually led to a sharp aggravation of the inflationary processes and to a chronic crisis of government finances. The neoclassics asserted that the economy was basically "healthy" and had no need of massive action on the part of the government, so that government interference in the economy had to be reduced.

The discussions over the potentialities for the self-regulation of the capitalist economic mechanism concentrated on the role of money in the processes of reproduction. The neoclassics argued that the monetary system was a key mechanism ensuring the automatic correction of effective demand over the long run. By contrast, the neo-Keynesians held that the functioning of money was a factor which tended to "unhinge" the system, and was an instrument of discretionary government control.

This chapter contains a critique of the basic tenets of the competing trends in bourgeois economics over the influence of money.

1. From Keynesian Theory to Monetarism

Keynes was the first bourgeois economist who openly admitted that capitalism was incurably ill and that it required active government measures to keep it running. Today, these views are opposed by the neoclassics, who insist that the government should not intervene in economic life.

The neoclassics deny the relevance of the Keynesian programme for stimulating aggregate demand and ensuring full employment on the plea that Keynes's model does not accord with the actual processes of capitalist reproduction.[1]

The current anti-Keynesian campaign is not something totally new in the history of Western

[1] The US economist Sumner H. Slichter published back in the late 1950s an article under the characteristic title:

economic doctrines. Back in the late 1930s, Keynes's theory was strongly opposed by the most conservative bourgeois economists, ranging from the "second generation" of the Austrian School (L. von Mises, F. A. Hayek) to the US neoliberals (W. Simon and H. Hazlitt, among others), who presented Keynesianism as being just short of a "camouflaged socialism" aimed against the key institutions of capitalist society.[1]

The gradual reappraisal and reformulation of the ideas Keynes expressed in his *General Theory of Employment, Interest and Money*, which began back in the 1940s, was highly important for the fortunes of Keynesianism, for it was designed to reconcile these with the traditional neoclassical models of general economic equilibrium. Leading Western theorists like John Hicks, Lawrence Klein, F. Modigliani, and Paul A. Samuelson, worked to "enrich" Keynesian macroeconomic theory with elements of microanalysis.

The remodelling of Keynes's orthodox system reflected the profound dissatisfaction among Western theorists and economic policy practitioners with the state of economic analysis, which in many fields was at odds and in some was in direct contradiction with the modern trends in capitalist economic devel-

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"The Passing of Keynesian Economics", saying that "Keynes's theory has turned out to have been wrong in all its essentials", having in mind above all Keynes's conclusion concerning the law-governed nature of economic crises (S. Slichter, "The Passing of Keynesian Economics". In: *The Means to Prosperity*, Economica Books, Buffalo, 1959, p. 79).

[1] This view was opposed by the Keynesians, who emphasised their teacher's loyalty to the capitalist system and the interests of the bourgeois class: "Keynes was capitalism's defender against Marxism... At a time when the Great Depression put capitalism in jeopardy, Keynes rebuilt economics within, not outside, the capitalist framework... He kept an intellectual generation from going Communist" (Henry C. Wallich, "Keynes Re-Examined: The Man, the Theory". In: *The New York Times Magazine*, April 20, 1958, Section 6, pp. 13, 91-92).

opment. Thus, the idea of the "depressive economy", which runs through the whole of Keynes's theoretical model, logically led to the conception of "permanent stagnation" put forward by the leading US Keynesians Seymour E. Harris and Alvin Hansen. In accordance with this theory, most bourgeois economists predicted the beginning after the Second World War of a deep economic depression equal in scale and consequences to the 1929-33 crisis, something that did not, after all, occur.

In the 1950s and 1960s, despite painful crisis recessions, the capitalist economy entered upon a period of revival, which was characterised by a relative excess of demand instead of a shortage, as the Keynesians had predicted.

The "overheating" of the economy led to an inflationary boom. What is more, in the 1960s, the rise of prices became permanent, and developed into a global phenomenon which hit all the capitalist countries without exception, and which sharply aggravated the social and economic contradictions of capitalism. The task of containing inflation was brought to the fore in government stabilisation programmes in the 1960s and 1970s, and came to be regarded as Problem Number One in economic and political terms.

The 1970s brought new complications to the economic development of the capitalist world: despite all the canons of the Keynesian theoretical scheme, the rising prices in most capitalist countries did not indicate the attainment of "full employment". Inflation was closely interwoven with the most acute unemployment.

The neoclassics mounted an attack on Keynesianism along all the main lines of economic theory, a wave of criticism which economic writers in the West designated as the "neoclassical renaissance", an amorphous trend with an explicit ideological tenor and bringing together economists of the most diverse persuasions. Their common line appears to amount to a refutation of the idea of the chronic internal instability of the capitalist economy, which is claimed to be capable, even today, to ensure maximum output and employment without any government interference.

In the course of the "great debate" concerning the real importance of Keynesian theory, there was a rapid revival of the neoclassical theory of money. That was the area of most acute contradictions in Western economics of the recent period. Concern over inflation led to a growing popularity of the quantity theory of money, which after many years of decline and stagnation once again came on the scene as a rival of Keynesian theory.

Earlier on, in the 1930s, criticism of the postulates of the quantity theory had been a necessary prerequisite for the Keynesian break-up of the whole structure of neoclassical economics. Now, the very opposite situation has developed: a refurbished quantity theory is being used as a weapon for counter-attack against Keynesian doctrine and the standard macromodel of income formation which is dominant in present-day theoretic literature in the capitalist countries.

The "renaissance" of the quantity theory was most explicit in the theoretical conception of the Chicago School headed by the US economist Milton Friedman, who saw money as the mainspring that could cause fluctuations in the process of production but could at the same time act as a mechanism stabilising the capitalist economy. The Chicago School's motto "Money matters", which offered a peculiar clue to the works of its economists, was contrasted with the Keynesian doctrine (rather, with its "standard" version)[1], which, according to these economists, held that "money does not mat-

[1] Meaning a more general class of reproduction models in which the specific elements of orthodox neo-Keynesian doctrine (the "liquidity trap", etc.) are presented as a "special case".

ter" for economic growth. The monetarists claim that there is a close causal nexus between the fluctuation of money supply and prices, and propose a purely monetary conception of the causes behind inflation, and a monetary theory of the cycle. By contrast, Keynesian writings prefer non-monetary explanations of the price dynamics (for instance, the "cost-push" theory) and basically non-monetary approaches to income and employment.

The urge to rehabilitate the quantity theory, to restore the neoclassical view of money, and to use it for a special interpretation of the laws governing the functioning of the capitalist economy was also reflected in another line of "neoclassical renaissance", namely, the growing popularity of so-called neo-Walras models of general economic equilibrium, a trend presented most completely in the writings of Don Patinkin, who used the so-called Pigou effect to show the ways in which the economy automatically "adjusted" to the state of full employment. Here, the edge of neoclassical analysis is directed against the idea that capitalism has worked out its internal stimuli for dynamic development.

Critics of the orthodox Keynesian model and its subsequent modifications asserted that there was a flimsy basis to Keynes's idea that the economy could long remain in a state of depression or stagnation: if Keynes's assumption concerning the inflexibility of prices and wages in the present conditions were discarded, the economy would function according to "neoclassical laws", i.e., it would eventually enter into a state of full capacity.

It is true that most Western theorists were forced to admit, following intense empirical research, that the "wealth" effect on which the neoclassics based their refutation of Keynes's "depressive economy" was very weakly expressed in the actual conditions of capitalist reproduction, and could not ensure an automatic movement of the economy out of its state of crisis recession. Hence this eclectic conclusion: although the capitalist economy was, in principle, capable of self-regulation, there was a need to maintain government stimulation of demand in order to speed up the economic correctives. The Keynesian scheme was, consequently, recognised as a peculiar "catalyst" of stabilising processes, rather than as a reflection of the essential features of the economic mechanism.

For their part, in the late 1960s and early 1970s, the Keynesians mounted a counter-offensive against the neoclassics, seeking to prove that Keynes's theory, being the model of a "disequilibrium economy" differed substantially from the neo-Walras model. That is why, the neo-Keynesians asserted, "neoclassical synthesis" as an attempt to reconcile Keynes and the "classics" was incorrect at root. It was not accidental departures from equilibrium, but the internal workings of the capitalist economy that kept the economic system in a state of underemployment. Keynes's analysis, they said, laid the basis for a study of the "disequilibrium situations" typical of capitalism (crises, inflation and other disruptions of reproduction), while in the models of neoclassical synthesis these phenomena are presented as being accidental and easily removable.

Once again the polemics largely centred on monetary problems. First, the US economists John G. Gurley and Edward S. Shaw criticised the basic premises of Patinkin's model as being artificial and not in accord with reality. Then followed the works of R. W. Clower and a book by A. Leijonhufvud, presenting a new interpretation of Keynes's basic ideas in general economic theory, and especially in monetary theory. They insisted that underemployment of resources organically sprang from the presence in capitalist exchange of a specific commodity—money—and that it substantially limited and hampered the potentialities of realisation. They argued that the Walras-type neoclassical models attain complete coordination and free realisation of commodities through an artificial identification of money with conventional goods.

The present-day Keynesians' "monetary economy" is as weak a construct as the neoclassical models of general equilibrium. What is common to the approach of Western theorists, whatever their school, is their neglect of the qualitative features of the capitalist relations of production and the bourgeois laws of property and the distribution of income, the true source of conflicts and contradictions in the capitalist world. Let us note, however, that in stressing the inevitability of these contradictions and the absence of any conditions for "harmonious development" under present-day capitalism, the Keynesians have moved closer to assessing the realities than the neoclassics, whose views are based on models of general economic equilibrium.

2. Apology of Capitalism by Chicago School Theorists

The doctrine of monetarism. The publication in the United States in 1956 of a collection of essays[1] under the editorship of Professor Milton Friedman of the University of Chicago marked the birth of a new theoretical doctrine, now claiming to be the theoretical antipode of neo-Keynesianism. In his introduction, Friedman formulated a special version of the quantity theory of money, a new version of the "monetary view" of the performance of the capitalist economy. This was followed by a series of empirical statistical studies to develop and polish up the new theory.[2]

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[1] *Studies in the Quantity Theory of Money*, Ed. by Milton Friedman, The University of Chicago Press, Chicago, 1956.

[2] See: Milton Friedman, Anna J. Schwartz, *A Monetary History of the United States. 1867-1960*, Princeton University Press, Princeton, 1963; Milton Friedman *A Program for Monetary Stability*, Fordham University Press, New York, 1960; Milton Friedman, *The Demand*

The monetarists assert a totally new view of the general nature of the capitalist economic mechanism and its capacity for effective self-regulation. Karl Brunner declares:

> "The monetarist position thus denies the proposition that the dynamic process governed by the private (non-governmental—*V.U.*) real sector is unstable over some major ranges."[1]

Another active monetarist, Leland B. Yeager, writes: "Certain unsatisfactory aspects of the performance of the capitalist economy—inflation, recession, cyclical unemployment, and balance-of-payments crises—*are not characteristic of capitalism itself* but result, instead, from a defective monetary policy; and monetary policy is a government function"[2]. This is echoed by Leonall C. Andersen and Keith M. Carlson, who write:

> "The economy is basically stable and not necessarily subject to recurring periods of severe recession and inflation. Major business cycle movements that have occurred in the past are attributed primarily to large swings in the rate of growth in the money stock."[3]

The global strategy of the monetarist conception is quite clear, and coincides with the over-all ten-

for Money: Some Theoretical and Empirical Results, New York, Occasional Paper 68, 1959; Milton Friedman, Anna J. Schwartz, "Money and Business Cycles". In: *The Review of Economics and Statistics*, Vol. XLV, Supplement, February 1963, and a number of works by Friedman's followers, among them Phillip Cagan, David Fand, Richard Selden, and David Meiselman.

1 K. Brunner, *The "Monetarist Revolution" in Monetary Theory*, Weltwirtschaftliches Archiv, Ed. 105, 1970, Part 1, p. 6.

2 Leland B. Yeager, *Monetary Policy and Economic Performance*, American Enterprise Institute, Washington, 1972, p. 13 (emphasis added).

3 Leonall C. Andersen and Keith M. Carlson, "A Monetarist Model for Economic Stabilisation". In: *Federal Reserve Bank of St. Louis*, April 1970, Vol. 52, No. 4, p. 8.

dency of the current "neoclassical renaissance" to rehabilitate "classical" capitalism, to revive faith in its efficiency and in the possibility of economic growth without additional "props" or government-budget stimulation. Hence the negative attitude to the Keynesian programmes for regulating demand, since these, the monetarists claim, disrupt the natural process of economic correctives through competition and free price formation.

This brings out one of the most important features of the neoclassical criticism of Keynesianism, namely, the demand to set definite limits to government intervention in the economy, and to eliminate the forms of intervention which to some extent do not meet the interests of big business and which, for that reason, are seen as a threat to free enterprise. Budget appropriations for the population's social needs are the most frequent targets of attack.

For some time now, Friedman has been advocating a cardinal restructuring of the fundamental principles of economic policy for the purpose, in particular, of depriving state-monopoly agencies of economic control of the freedom of manoeuvre they now have, and in order to subject their activity to the automatic "rule" which takes into account long-term economic trends.

The monetarists believe that the "instability" of capitalism is rooted in the monetary sphere, and that is where one should look for the main causes of crises and other disruptions of the reproduction process.[1]

Monetarism was a peculiar response to the long

[1] Yeager wrote: "A monetarist is an economist convinced by the evidence that the quantity of money and changes in it dominate the total flow of spending in an economy. The government budget, and so-called real factors in the economy, including investment incentives, are distinctly subordinate influences when not paralleled by behaviour of the money supply" (Leland B. Yeager, *Monetary Policy and Economic Performance*, American Enterprise Institute, Washington, 1972, p. 27).

period in which monetary factors in the economic processes of the capitalist countries were ignored throughout the 1930s and 1940s. Friedman started the "re-evaluation of values" in the bourgeois interpretations of the role of money. He wrote:

> "It was a theoretical approach that insisted that money does matter—that any interpretation of short-term movements in economic activity is likely to be seriously at fault if it neglects monetary changes."[1]

The idea of the extraordinary role of money and the fatal consequences of underrating this factor became the starting point for the offensive against Keynesian positions.

There is some realism in the view that "money matters for economic development", but in the monetarists' postulates it assumes a distorted and hypertrophied form. James Tobin observed that they tend to present the "money matters" motto as "money is all that matters"[2]. The monetarists regard money as the basis not only for theoretical analysis but also for economic prognostication and as the chief instrument of government economic policy. This approach essentially differs in substance and conclusions from Keynesian-type models which emphasise the dynamics of economic factors like investment, consumer spending, and savings, and which emphasise stimulating fiscal policy pursued by the government.

Monetary doctrine has gone through several stages of development. Friedman began by rehabilitating the quantity theory of money and reformulating its basic propositions. He borrowed some im-

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[1] *Studies in the Quantity Theory of Money*, Ed. by Milton Friedman, the University of Chicago Press, Chicago, 1956, p. 3.

[2] James Tobin, "The Monetary Interpretation of History". In: *The American Economic Review*, Vol. LV, June 1965, No. 3, p. 481.

portant ideas from the works of Irving Fisher, a well-known advocate of the quantity theory in the early years of this century, and from the Cambridge theorists, although his interpretation of the quantity theory markedly differs from the traditional versions in premises, analytical apparatus, and form of exposition.[1]

Friedman's early works contain references to the "oral tradition" of the Chicago School, where a system of monetarist views had allegedly long existed and was being polished up. Subsequently, Patinkin scrupulously analysed the lectures given by members of that school at the University of Chicago in the 1920s, 1930s and 1940s, and showed that they had held to the orthodox version of the quantity theory based on Fisher's equation of exchange.[2] Still, the Chicago School is a term that is broadly used today to characterise the views of Friedman and his colleagues.

Monetarist schemes have had a marked influence on economic-policy conceptions and the practical measures taken by government agencies in some capitalist countries (Britain, FRG, and Japan, as well as the United States). This influence was most pronounced in the late 1960s and early 1970s, when there was a sharp spurt in the inflation. The application of monetarist recipes for limiting effective demand on a large scale has shown up their anti-democratic nature, and has led to a marked aggravation of the social contradictions of capitalism. The slow-down of monetary and credit expansion in the United States and the active use of monetary restrictions as an anti-inflationary instrument in

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[1] See: Milton Friedman, *The Counter-Revolution in Monetary Theory*, Wincott Foundation, London, 1970, pp. 8-11; also his "A Theoretical Framework for Monetary Analysis". In: *The Journal of Political Economy*, March-April 1970, pp. 195-201.

[2] See: Don Patinkin, "The Chicago Tradition, the Quantity Theory, and Friedman". In: *Journal of Money, Credit and Banking*, February 1969, pp. 46-70.

1969 and 1970 sparked off a "deflationary crisis", with a growth of unemployment and external economic and monetary difficulties. Government agencies in the United States, Britain and other capitalist countries, where monetarist recipes of money management were being vigorously applied, were forced to return to the Keynesian policy of demand stimulation.

This caused some disappointment with the practical application of monetarism, but the set of monetarist ideas is still very popular among bourgeois economists and is the basis for conservative recommendations on policy matters.

The monetary theory of the economic cycle. We have seen that the monetarists regard the capitalist economy as an inherently stable system which is typical in a state of smooth and balanced growth, while crisis phenomena like recessions, unemployment, inflation, and other disturbances are accidental and irregular. They say that the main cause of these crisis phenomena lies in the chaotic fluctuations of money supply, which, for its part, is caused by government manipulations to stimulate aggregate demand, etc.[1]

Thus, the source of economic instability is transferred to the "external sphere" and the fact that this instability is inherent in the capitalist system is camouflaged.

The monetary theories of the cycle have always had a prominent place in the history of bourgeois economic thinking, being most widely accepted at

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[1] The US economist Hyman P. Minsky described the monetarist approach as follows: "The observed path of money income and prices is interpreted as the result of shocks imposed upon an otherwise inherently stable growth process by random or systematic changes... The introduction of a money supply that behaves in the correct manner would eliminate either all or at least a large part of those disturbances that constitute the major malfunctioning of an enterprise system." (*The State of Monetary Economics*, New York, 1963, p. 66).

the turn of the century as expounded in the works of R. G. Hawtrey, Knut Wicksell, F. A. Hayek, L. von Mises, and Irving Fisher. Present-day monetarists emphasise the historical continuity of their works, with references to Fisher's well-known article in which he identified the cycle with the "dance of the dollar", i.e. the changes in the purchasing power of money.[1] But the essential distinction is that the early monetarists believed that fluctuations in production were caused primarily and mainly by banking operations, credit terms, etc., that is, advocated what essentially amounted to a "credit" concept of the cycle, whereas the present-day monetarists offer a "purely monetary" approach, believing the phenomena of the credit market to be secondary and supplementary.

The idea that monetary factors have a decisive influence on the general economic processes is the main subject of the widely popular book by Milton Friedman and Anna Schwartz.[2]

Their line of argument is based on historical parallels and analogies in the dynamics of some indicators. Thus, when mentioning the two "major price inflations" (meaning the consequences of the First and Second World wars) they accentuate the fact that on both occasions inflation went hand in hand with a more than twofold increase in money supply. Furthermore, in the almost 100 years under review there were six cases of "deep economic depression", each of which was preceded by a considerable reduction in money supply. From these comparisons they draw the conclusion that there is a close connection between the cyclical fluctuations of money supply and the changes in real income or business

[1] Irving Fisher, "The Business Cycle Largely a 'Dance of the Dollar'". In: *Journal of the American Statistical Association*, December 1923.

[2] Milton Friedman, Anna J. Schwartz, *A Monetary History of the United States. 1867-1960*, Princeton University Press, Princeton, 1963.

activity, and that over the long term the essential instability of money is accompanied with the instability of economic growth.

They realise, of course, that the existence of a correlation in the dynamics of monetary and other economic factors does not at all prove that these phenomena are connected as cause and effect, but keep saying that it is the "instability of money supply" that is to blame for the major economic slumps.

In their efforts to prove that the influence coming from money to economic activity has prevailed, and that money has played the role of senior partner, they put a specific interpretation of various episodes in the history of the Federal Reserve System (FRS), like its increase of the discount rate in 1920 from 4.75 per cent to 7 per cent; a similar increase in October 1931, from 1.5 to 3.5 per cent, and finally, a doubling of the reserve requirements in 1936-37. Friedman and Schwartz say that all these acts had a clearcut and unequivocal effect: they caused a reduction in the money supply (respectively by 9.14 and 3 per cent), which was followed by three sharp drops in industrial production (by 30, 24 and 34 per cent).

Even their opponents were shocked by such a one-sided and flimsy interpretation of the causes behind the economic cycle. Of course, the disastrous consequences of a slump are closely connected with monetary processes, but Friedman and Schwartz did not confine themselves to indicating the importance of money in the aggravation of economic crises. They insisted that monetary factors were the chief and virtually the only cause of the cyclical fluctuations in economic activity.

In this context, it is interesting to follow their analysis of the causes of the deep crisis of 1929-33. They present it as the outcome of a series of fatal mistakes made by the US central bank, and declare that all of its actions during that period were harmful: it should not have combated the speculative boom on the stock market (although its collapse in 1929 showed the serious danger of riotous speculation in stocks); it should not have helped the commercial banks in the form of rediscounting, because this merely postponed the fatal outcome (despite the fact that thousands of banks were forced to stop payments); its operations on the open market were not sufficiently large-scale (although in 1932 alone, the FRS purchased government bonds for the amount of 1 billion dollars, and so on. By its hesitant and passive policy, the FRS allowed the money stock to shrink over a long term, and that was the cause of the disaster.

While emphasising the role of monetary, psychological, administrative, and other elements, the monetarists fail to take into account the fact that the 1929-33 monetary and credit crisis was not a common episode which grew to ugly proportions because of poor decisions on the part of US economic policy leaders, but was a specific form of violent resolution of actual economic disproportions and social contradictions that had built up in the period of "prosperity" (overaccumulation of industrial capital, excessive growth of the credit superstructure, the speculative boom on the stock market, etc.). Nor do they reckon with the fact that the crisis in the United States was an important element of a world economic crisis, which hit all the countries of the capitalist world.

Friedman and Schwartz tried to compensate their one-sided approach by referring to the "bilateral" relation between money and economic stability, by recognising the impact of non-monetary factors in some cases, etc. Their arguments are frequently so equivocal that it is just as hard to catch them out as to "nail down a piece of jelly to the wall", as one critic put it. Whenever any monetary actions precede changes in the situation, the authors claim this to be proof in their favour; whenever monetary changes fail to have an effect, they refer to the "distorting influence of non-monetary factors".

The method of formal statistical comparisons couched in the traditions of the institutionalist school, a method which has been very popular in the work of the National Bureau of Economic Research for many years, is also used by Friedman and Schwartz in an article entitled "Money and Business Cycles"[1]. In this article they give a more detailed analysis of the correlation between the US money supply and national income than they did in their *Monetary History*, with emphasis on a comparison of the turning points in the cyclical fluctuations of these indicators during more than twenty periods of sharp slumps in industrial production from 1869 to 1960.

They draw attention to the fact that the turning points in the money dynamics as a rule preceded the turning points in the economic situation. From this they draw the conclusion that

> "appreciable changes in the rate of growth of the stock of money are a necessary and sufficient condition for appreciable changes in the rate of growth of money income"[2].

Meanwhile, J. Tobin showed that these facts were compatible with the most diverse hypotheses concerning the interaction of economic factors and that "cyclical leads of money over money income say virtually nothing about direction of causation"[3].

Still, Friedman insisted on his version of the causes behind the cycle, claiming that "the major direction of influence is from money to business",

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[1] Milton Friedman, Anna J. Schwartz, "Money and Business Cycles". In: *The State of Monetary Economics*, National Bureau of Economic Research, New York, 1963.

[2] *Ibid.*, p. 53.

[3] James Tobin, "Money and Income: Post Hoc Ergo Propter Hoc?" In: *The Quarterly Journal of Economics*, Vol. LXXXIV, May 1970, No. 2, pp. 301-317).

and that this was the "key element in monetary theory of cyclical fluctuations"[1].

Money, interest, and prices: the "transmission mechanism" in monetary processes. The weakest point of the monetarist doctrine is the question of the mechanism by which money influences the performance of the economic system.

Western economic writers have repeatedly criticised the works of Friedman and his colleagues for having failed to consider the main aspect of the pivotal problem: if the money-supply dynamics is the main cause of the cycle, what are the channels and forms in which its influence is transmitted to the other key economic processes? How is a reduction in "money supply" transformed into a drop in production, and its increase, into a growth of production?

According to Keynes, the "transmission mechanism" of the influence of money is based on changes in interest rate. Interest is introduced into the economic model in two ways: as an argument of the liquidity preference function (which has an influence on the demand for cash balances) and as an argument of the investment function (which determines the rate of investment). Accordingly, much importance is attached to the elasticity of both functions with respect to interest. On this depends the final effect of money.

In the monetarist scheme, interest rate is not regarded as the key factor in the connection between "real" and monetary processes. In the consideration of the mechanism of economic adjustments, the emphasis is on changes in the structure of the "portfolio balance", which includes a wide range of accumulated assets (money, bonds, real capital, consumer durables, etc.). It is always the money supply that "triggers off" the changes in this struc-

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[1] Milton Friedman, "Comment on Tobin". In: *The Quarterly Journal of Economics*, Vol. LXXXIV, May 1970, No. 2, pp. 321, 326.

ture. Monetarist analysis assigns to money factors the chief place among all the other impulses which influence the economic process, and so rejects Keynes's hypothesis concerning the extraordinary importance of investment; the fluctuations of production round the long-term trend are connected with rates of changes in money supply, but this influence manifests itself with a long and changing lag.

The stability of the function of demand for money has a major place in this "transmission mechanism" model. Present-day monetarists hold to the Cambridge version of quantity theory, according to which there is a stable proportion between money supply and income. A disruption of this proportion, caused by the haphazard changes in money emission (as a result of central bank policy) upsets the "portfolio balance". Accordingly, money is said to be the key cause behind the fluctuations in economic activity.

According to Friedman, whenever the volume of cash balances changes under the impact of some external factors, economic agents respond to it by a change in the structure of their assets and liabilities. This will change the relative prices of different assets and the rate of income they yield. This will cause changes in consumer and investment spending, i.e. factors which, according to the generally accepted scheme, shape the magnitude of the final product. Friedman's conclusion is that the effect of monetary changes will ripple through, so that many of its main consequences will be evident only months after the initial disruption.

The monetarists' treatment of interest deserves special consideration. Friedman establishes three possible versions of temporary fluctuations in the rate of interest: 1) "liquidity effect", 2) "income effect", and 3) "anticipation effect" (anticipation of price changes).

The "liquidity effect" is connected with the initial phase in the disruption of the "portfolio balance" resulting from a change (say, an increase) in money supply. The excess money (as compared with the "habitual" level) induces the owners of cash balances to intensify their purchase of securities, which leads to a rise in their price and so reduces their actual yield.

But that is only the initial response. A reduction in interest will lead to a growth of income and, in consequence, to a growing demand for loan capital. That is the second stage, in the course of which interest rates will once again rise to the old level ("income effect").

The third effect ("price anticipation effect") may push the interest beyond the old limits. This effect is connected with Fisher's idea that market ("nominal") interest consists of two components: "real" interest, which is determined by the factors of demand for capital and its supply, and a "premium", which depends on the expected rate of price changes. So, according to Fisher, in a period of rising prices, creditors seek to include in the interest charges the losses occurring through the depreciation of the principal; in periods of stable prices, the "premium" is not exacted and, consequently, the "real" and the "nominal" interest rates coincide.[1]

Thus, the monetarists believe that the rate of interest tends to rise when the money equilibrium is upset mainly because of changing prices. A rise in income will be accompanied with a growth of prices. There is an anticipation of their further rise, and so creditors seek to "insure" against the depreciation of money, adding to the interest rate the expected price changes over the loan period.

The monetarist scheme gives an extremely superficial and distorted reflection of the actual processes of capitalist reproduction. It abstracts from many

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[1] Irving Fisher, *Appreciation and Interest*, Andrus & Church, New York, 1896; also his: *The Theory of Interest*, The Macmillan Co., New York, 1930.

very important processes in which the value and use value of commodities are created on the basis of exploitation of labour, from turnover of social capital in its diverse forms, from the exchange between the two departments of social production in its physical and value composition, and from many other problems which are necessary to analyse capitalist reproduction.

This method of economic analysis is highly convenient for an apology of capitalism, for it helps to evade the problems arising from class stratification and social inequality, the capitalist forms of exploitation and oppression, and other issues which are "dangerous" from the standpoint of bourgeois ideology. The "switches" of incomes derived from the various types of financial and real assets are no more than external perturbations which do not change but merely follow the general trends of capitalist reproduction.

The monetarist view of "nominal income". The "extraordinary importance" of money is curiously laced in the works of the monetarists with the traditional conclusion of quantity theory that money factors are inessential over the long run, and that they mainly influence the "price veil". This dichotomy gives rise to a real contradiction in assessing the effect of government stabilisation measures: monetary and credit policy is regarded as the most powerful and effective instrument for exerting an influence on the economy, and this fails to square with the neoclassical view of money as a "veil".

In recent years, the monetarists have tried to eliminate this contradiction.[1] Friedman himself says:

[1] One of them writes: "Monetarists may have experienced difficulties in obtaining a wider understanding of their model ... because it seems to include, in one category, both the money veil of theory and the extremely potent highpowered money of stabilisation policy." (David I. Fand, "A Monetarist Model of the Monetary Process". In: *The Journal of Finance*, Vol. XXV, May 1970, No. 2, p. 279.)

> "The key source of misunderstanding about the issue of monetary policy, in my opinion, has been the failure to distinguish clearly what it is that money matters for... The quantity of money is extremely important for nominal magnitudes, for nominal income, for the level of income in dollars... important for what happens to real output over the long period."[1]

Friedman uses the "monetary theory of nominal income" to produce a theoretical generalisation of his view on the connection between money and money factors.

Friedman says that money factors have an impact on the production of commodities (in other words, on the physical component of the national income) only in the short run, but all his statements about this effect are extremely obscure and vague.[2]

Friedman makes sure that his formulations are never clearcut, which gives him room for manoeuvre when his theories are at odds with the actual processes.

In the recent period, under the influence of criticism from rival schools, the monetarists have been forced to produce a more clearcut structural model reflecting their notions about the key interrelation-

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[1] Milton Friedman, Walter W. Heller, *Monetary vs. Fiscal Policy*, W. W. Norton & Company, New York, 1969, p. 46.

[2] Thus, in a lecture in London in 1971, he starts out by saying that the influence of changes in money supply is expressed above all in the sphere of real production (with a lag of 6-9 months) and only then in price changes with a lag of another 6-9 months). But then, in the same lecture, he says that this influence is drawn out over a period of years: "In the short run, which may be as much as 5 or 10 years, monetary changes affect primarily output. Over decades, on the other hand, the rate of monetary growth affects primarily prices." (Milton Friedman, *The Counter-Revolution in Monetary Theory*, Wincott Foundation, London, 1970, pp. 22-24.)

ships in the economy, and Friedman did this in two long articles.[1]

The first begias with the key point of quantity theory, by drawing a dividing line between "nominal" and "real" (deflated) economic variables.

In Keynesian-type schemes this distinction is often ignored, because the price level over the short term is assumed to be fixed, so that the real magnitudes of the factors of reproduction being transformed into money prices are not changed. By contrast, in the monetarist model, economic agents are not oriented upon "nominal" money balances, not on a simple quantity of money units, but on the stock of money evaluated in accordance with its actual purchasing power. Changes in the "nominal" balances have an effect on the value of money through the mechanism of demand and prices, and this, for its part, generates a process of economic correctives which result in a fluctuation of the final product, which is once again no more than a "nominal" product, that is, commodities expressed in terms of money. Consequently, the role of money is ultimately reduced to the changes in prices.

Friedman claims that prices are the chief instrument for correcting the market situation, because prices adjust faster than the quantities of commodities exchanged in the market, indeed, so fast that the price correctives may be regarded as instantaneous.[2] By contrast, Keynes's mechanism of price adjustment runs so slowly (in virtue of institutional and other factors) that it can be ignored altogether, assuming prices to be unchanged over the short term.

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[1] Milton Friedman, "A Theoretical Framework for Monetary Analysis". In: *The Journal of Political Economy*, Vol. 78, No. 2, March-April 1970, pp. 193-238; also his "A Monetary Theory of Nominal Income". In: *Monetary Theory and Monetary Policy in the 1970's*, Proceedings of the 1970 Sheffield Money Seminar, Oxford University Press, London, 1971, pp. 41-71.

[2] Milton Friedman, "A Theoretical Framework...", p. 222.

For a comparison of the "oversimplified" Keynesian and the monetary doctrine, Friedman offers the following model consisting of six equations:

$$\frac{C}{P}=f\left(\frac{Y}{P}, \quad r\right), \tag{1}$$

$$\frac{\dot{I}}{P}=g(r), \tag{2}$$

$$\frac{Y}{P}=\frac{C}{P}+\frac{\dot{I}}{P}\left(\text{or } \frac{S}{P}=\frac{Y-C}{P}=\frac{\dot{I}}{P}\right) \tag{3}$$

$$M_d=P\cdot l\left(\frac{Y}{P}, \quad r\right), \tag{4}$$

$$M_s=hr, \tag{5}$$

$$M_d=M_s, \tag{6}$$

where C is consumer spending; $\dot{I}$ investment; P price level; Y gross final product; S savings; M_d money demand; M_s money supply; and r rate of interest.

Equations (1)-(3) describe the "real" sector, taking into account the factors of consumption, investment, and savings; equations (4)-(6) describe the money sector. Equation (1) is the consumption function, where consumption is connected with the level of real income $[(Y/P) = y]$ and the interest rate (r). Equation (2) expresses real investment as a function of the interest rate. Equation (3) is an identity, which specifies the condition of equilibrium in the "real" sector (investments equal savings).

Equation (4) is the function of the money demand, where the level of nominal money balances depends on real income, prices (P), and interest rates; equation (5) determines the money supply, and (6) gives the condition for equilibrium on the money market.

Friedman believes that the model is acceptable in principle both for those who advocate the quantity theory and for Keynesians, with the following differences: the model is incomplete, because six equations contain seven unknown variables (C, I, Y, r, P, M_d and M_s), so that there is a need for another equation with the lacking variable introduced exogenously.

The advocates of quantity theory "close" the system by means of this equation:

$$Y/P = y = y_0. \tag{7}$$

In other words, the magnitude of "real" income, its physical component, is determined outside the model, and so the number of unknown variables is reduced to six. This, in effect, amounts to the acceptance of the "classical" premise of full employment.

According to Friedman, the Keynesians need to add another equation:

$$P = P_0. \tag{8}$$

Here, it is the price level, assumed to be stable, that is determined outside the model. In other words, this is the introduction of the traditional Keynesian premise of "nonelastic" prices, which are determined by institutional factors.

What are the results of these transformations?

If $Y/P = y_0$, the subsystem of the first three equations of the model becomes autonomous and on its own determines the three "real" variables (C/P; I/P and r). The equation of money demand in the money market sector takes the form of Fisher's equation of exchange which determines the "price veil".

In the event of the Keynesian solution ($P = P_0$), equations (1)-(3) begin to determine the relation between interest rate and the level of nominal income in the "real" sector. Simultaneous solution of all six equations determines the equilibrium level of interest rate and "real" income.

Both solutions represent the abstract logical approach to the problem which is based not on real economic developments but on some arbitrary assumptions. The advocates of quantity theory assume a constant physical volume of output (the case of "full employment"), and Keynesians, assume a constant price level. Neither of these approaches can say anything about the factors which determine the proportion in which the short-term changes in nominal income are divided between prices and physical output.

Friedman's article caused great disappointment among his followers: it clearly showed that despite the years of polemics against the advocates of the standard macroeconomic model, he had no original approach of his own and that only the assumption of "full employment" in the real sector helped to reduce the influence of money on the changes in prices.

Apparently in view of this unfavourable response to his first article, Friedman subsequently proposed another model, in which the "nominal" income is not devided into physical and value components. It consists of four equations:

$$M_d = Y \cdot l\ (r), \qquad (4a)$$

$$M_s = h\ (r), \qquad (5a)$$

$$M_d = M_s, \qquad (6a)$$

$$r = K_0 + \left(\frac{1 \cdot dY}{Y\, dt} \right). \qquad (9)$$

The changes made in the equations are insignificant: in equation (4a) "real" income is replaced by "nominal" income; equations (5) and (6) are unchanged; and equation (9) has been added to determine interest rate. Here Friedman makes use of the ideas of Keynes and Fisher: from the former he borrows the idea that current interest is linked to a rate that may be assumed to prevail in the future; from the latter, the idea that interest rate takes into account the expectations about the rate at which commodity prices will change in the future.

Friedman admitted that the final effect of his model did not differ from that produced by the earlier one, but said that its "merit" lay in the fact that it did not even raise the question of dividing nominal income into value and physical components. In other words, instead of explaining the key aspect of the differences, Friedman simply dismisses the problem.

All these theoretical constructs are designed to strengthen the quantity theory of money and the monetarist version of the economic cycle based on it. The "nominal income" model contains all the chief components of monetarist doctrine: the neoclassical function of money demand, which establishes a direct relation between the demand for cash balances and the magnitude of money income; the exogenous money supply; and the specific monetarist version of the mechanism underlying the dynamics of interest (depending on changes in the price level). But it leaves aside all (or nearly all) of the most important and significant phenomena in the sphere of capitalist reproduction, without which it is impossible to analyse in a satisfactory way the main problems of economic development. Moreover, Friedman's theoretical model is not adapted to describing and analysing the effects produced by the mechanism of government economic policy.

3. The "Wealth Effect" and the Mechanism of Capitalist Reproduction

The amount of assets as a factor of economic behaviour. After the publication of Keynes's *The General Theory of Employment, Interest and Money*, neoclassical doctrine was plunged into a state of shock for a long time. The chief stabilising mechanism in the neoclassical model (flexible prices and wages balancing out supply and demand on all markets and, above all, on the labour market) had been switched off by Keynes's assumption of a "fixed" level of prices.

At the same time, the neoclassical argument bore mainly on factors regulating commodity supply. Thus, a fall of wages in the depression periods ensured, they believed, that employment would be maintained at its previous level and that a drop in commodity production would not develop. But Keynes asserted that it was not the volume of *commodity supply*, but *effective demand* that was the key factor limiting production. Whatever the level of supply, a shortage of demand will reduce production, employment, and income.

If the logic of the Keynesian concepts was to be formally refuted, there was a need to find within the system of capitalist economic relations an automatic "generator" of consumer demand that would compensate for the chronic shortage of investment. This role in the neoclassical scheme was gradually assigned to the "wealth effect", i.e. the relationship between consumer spending and the volume of assets accumulated by economic agents.

In the consolidated balance of the private (non-governmental) sector of the economy, statistics brings out the following: on the asset side, the amount of material and financial assets, and on the liabilities side, the debt liabilities and net worth. The latter element, which is obtained by deducting the economic units' total liabilities from their assets, constitutes the amount of "net wealth". Economically, this magnitude is the stock of real capital accumulated as a result of saving. When it comes to the balance of the private sector, this stock includes the amount of money representing the net liability of the government sector to the private one.

The hypothesis that the amount of accumulated assets could influence economic behaviour is not a new one, and echoes of it will be found in the works of A. Marshall. Some remarks on this matter also occur in Adam Smith's *An Inquiry into the Nature and Causes of the Wealth of Nations*. But the idea of the stabilising influence of revaluations of assets in various stages of the trade cycle was clearly expressed only by Gottfried von Haberler in his *Prosperity and Depression*, in which he described a phenomenon which was subsequently called the "Pigou effect" (or "real balance effect")[1].

First of all it concerns the reappraisal of the money element of accumulated wealth (money hoards) when prices tend to fall in a depression. Haberler used the well-known fact that a decline in commodity prices simultaneously results in an "appreciation" of money, a rise in its purchasing power with respect to commodities. Economic agents, feeling that they are "richer" (in the sense that the real purchasing power of the money stock will be higher than the habitual or normal level and, consequently, will in a sense be excessive), begin to limit their money hoards. So the larger part of the income will be spent on consumption. As a result, Haberler believes, additional demand is generated on the commodity market, which will automatically help the economy to pull out of the economic crisis.

Haberler also mentions in passing the possible effect of a drop in interest rate as a result of growing supply of loan capital in a depression. Back in 1951, the US economist L. A. Metzler pointed out that a revaluation of the portfolio of securities as a result of changes in the interest rate could be identical, in its final impact on consumption, to the changes in money supply, and that a rise in the yields on securities reduces the propensity to save, so increasing consumer spending.[2]

Western writers now use a common term, "wealth effect", to designate two phenomena: changes in

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[1] Gottfried von Haberler, *Prosperity and Depression*, Harvard University Press, Cambridge, Massachusetts, 1958, pp. 388-390.

[2] Lloyd A. Metzler, "Wealth, Saving, and the Rate of Interest". In: *The Journal of Political Economy*, Vol. LIX, April 1951, No. 2.

consumer spending under the impact of a spontaneous revaluation of the money components of wealth as a result of changes in prices and changes in consumer spending under the impact of a revaluation of securities as a result of changes in the market interest rates.

The consumption function which takes this effect into account is written in the following form:

$$C/P = C\ (Y/P,\ r,\ w/P), \tag{1a}$$

where C/P is the magnitude of real consumer spending (taking into account price changes); Y/P real income; r interest rate; and w/P total real accumulated assets, including money. (Let us recall that only the first argument, Y/P, will be found in the traditional Keynesian version of the function).

Pigou used Haberler's idea to question Keynes's conclusions concerning the basic instability of the capitalist economy.[1] He made the suggestion, which was then taken up by many neoclassical economists, that a reduction of prices and wages in an economic depression automatically stimulates consumption and reduces savings. This, he said, made it impossible for the economy to remain for a long time in a state of underemployment. Pigou's line of argument subsequently became a central method of the neoclassical criticism of Keynes's conclusions.

Most Western economists did not risk directly to recommend as a practical measure for eliminating crises the recipes which logically followed from Pigou's scheme, namely, a reduction in prices and wages through deflationary policy. The fact is that Western economists associated a fall in prices with a state of depression, so that advocating a policy of "price depression" would be tantamount to urging a stimulation of crisis processes. Up until the

[1] A. C. Pigou, "The Classical Stationary State". In: *The Economic Journal*, December 1943, pp. 343-351; also his "Economic Progress in a Stable Environment". In: *Economica*, Vol. XIV, No. 55, August 1947, pp. 180-188.

Second World War, such recommendations were deemed unacceptable for political reasons, which is why practical anti-crisis programmes continued to be the Keynesians' main trump card: the government was advised to step up credit and money emission so as to compensate for the inadequate demand.

After the war, bourgeois economists began to give increasing attention to the "Pigou effect" (and to the "wealth effect" as a whole) and included these in their theoretical schemes mainly out of the ideological urge to prove that capitalism was, in principle, a stable economic system.

Thus, the US economists Boris P. Pesek and Thomas R. Saving said in their book about the "wealth effect" that the conclusion that even a highly competitive economy was unable to reach full employment without government intervention "proved disturbing to many economists"[1]. Meanwhile, once the "wealth effect" is brought into economic analysis, it is tantamount to declaring that "we do not *have* to have the government, as a *deus ex machina*, to rescue us"[2]. At the same time, these economists asserted that in order to materialise, this effect requires elasticity of prices and interest rates.

> "If in any specific economy, such rigidities do exist, a removal of unemployment may again be accomplished either by the removal of them or by the application of government fiscal or monetary policy."[3]

Thus, contemporary theorists say that the capitalist economy can, in principle, be in a state of equilibrium even under full employment, but the greater the inflexibility of prices, the greater is the extent of government intervention required for the most rapid elimination of the equilibrium disruptions.

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[1] Boris P. Pesek, Thomas R. Saving, *Money, Wealth, and Economic Theory*, The Macmillan Co., New York, 1967, pp. 11-12.

[2] *Ibid.*, p. 14.

[3] *Ibid.*, p. 14.

This compromise, as it has been said, is characteristic of the stand taken by most present-day economists in the West.

In logical terms, the substantiation of the "Pigou effect" has serious defects. This hypothesis rests on a number of unrealistic assumptions concerning the behaviour of economic agents, like the premise that a revaluation of money supply in a depression will generate additional demand, because people will "feel themselves to be richer". Actually (if we exclude the stock-market tycoons buying up shares and enterprises at throw-away prices), the fall in prices during the period of inflated inventories of overproduction, mass bankruptcies, and unemployment cannot re-establish the shaken confidence and increase demand. The crisis entails a destruction of material wealth, so that economic agents will feel themselves to be poorer, not richer. In such a situation, the most typical trend is a further shrinking, rather than a growth of consumption, since the population will tend to save a larger part of their incomes for "a rainy day" in anticipation of economic hardships and growing unemployment. For a majority of the population, the fall in prices will most likely signal a worsening of the economic situation, instead of acting as an incentive for buying. This is a fact that many bourgeois economists have had to recognise, emphasising the weakness and unreliability of the "Pigou effect", the inadvisability of using it in practical policy, etc.[1]

The attempts to bring out by means of statistical calculations the existence and power of the "real balance effect" (like the other elements of the "wealth effect") have yielded rather contradictory results. Some economists, however, have reached the conclusion that the "Pigou effect" does exist (as a

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[1] See for instance: John M. Culbertson, *Macroeconomic Theory and Stabilisation Policy*, McGrow-Hill Book Company, New York, 1968, pp. 341-342.

rule, in the broader form of the "wealth effect" and with an eye to the influence of interest rate. on the revaluation of the securities portfolio)[1]s

Despite the absence of direct evidence concerning the influence of changes in real cash balances on the volume of demand, the "wealth effect" is being broadly used in theoretical models and is a prominent point in textbooks on macroeconomics and monetary analysis. The acceptance by bourgeois economists of the "wealth effect" has largely helped to spread the view concerning the theoretical weakness of Keynes's arguments for proving that the economic system could remain for a long time in a state of underemployment.

The Patinkin scheme and reality. A fresh impetus to the study of the "wealth effect" was provided by Patinkin.[2] Regarding money as a form of "net wealth", and using the "Pigou effect" as a key element of economic ties, Patinkin tried to give a well-defined substantiation of the neoclassical conclusion concerning the "neutral" role of money in economic development.

In his model, the behaviour of an economic individual is studied in a hypothetical situation, where he has a stock of commodities and money at the start of a given period. The scheme of the individual's market behaviour was borrowed by Patinkin from Hicks's model of general equilibrium.[3]

[1] See: Ta-Chung Liu, "An Exploratory Quarterly Econometric Model of Effective Demand in the Postwar US Economy". In: *Econometrics*, July 1963; J. S. Duesenberry et al., *The Brookings Quarterly Economic Model of the United States*. Chicago, 1965.

[2] Don Patinkin, *Money, Interest, and Prices*, Harper & Row Publishers, New York, 1956. The following of his articles were also important in backing up his model: "Relative Prices, Say's Law, and the Demand for Money". In: *Econometrics*, 1948; "Price Flexibility and Full Employment". In: *Readings in Monetary Theory*, London, 1952; "The Indeterminacy of Absolute Prices in Classical Economic Theory". In: *Econometrics*, 1949.

[3] See: J. Hicks, *Value and Capital*, London, 1946, Chapters 1, 2, 5, 9.

According to Patinkin's model, economic agents are forced to respond to any deviations of the actual money balances from the desired (required) level. Here is the main channel through which money influences the functioning of the economic mechanism. A disruption of the normal or habitual relation between the "real" stock of money and the amount of payments disturbs the equilibrium and produces a response on the part of the consumers which is eventually expressed on the commodity market. In the event of an excess of money balances over the "normal" level there arises an additional demand for commodities, so leading to a rise in prices. This process will continue until prices rise in exact proportion to the change in the real value of the money balances. Only then will equilibrium be established, i.e. only then will the forces causing the restructuring of prices disappear.

But that is precisely the "Pigou effect", namely, the dependence of consumption processes on a re-evaluation of "net wealth", whose role in this case is played by the money stock.

The publication of Patinkin's book in 1956 engendered many works on the "real balance effect" and its role in capitalist reproduction. The conclusions in these works are highly contradictory. Many economists were unable to discover the presence of this effect in the course of statistical analysis,[1] and others have found it to be so weak that it could well be neglected.

In a second edition of his book, Patinkin summed up the results of a large number of calculations of the consumer function in the United States, carried out by Lawrence R. Klein, C. F. Christ, K. A. Fox, Z. Griliches, and A. Zellner, among others. These calculations have produced a wide spectrum of values for regression coefficients with a real balance

[1] See: C. Schotta, "The Real Balance Effect in the US, 1947-1963". In: *The Journal of Finance*, 1964.

variable. The indicator of price elasticity of consumer spending to which special importance is attached as to an indicator of the strength of the effect, fluctuated within a range of —0.05 to —0.3; in most cases it came to —0.2. Patinkin gave a highly cautious assessment to these figures, pointing to the "considerable and puzzling variation in the results" and to the impossibility of judging "the validity of these conjectures", without additional information.[1]

The logic behind Patinkin's conception was equally vulnerable. The conclusion concerning the "neutrality" of money in his model can be reached only with the observance of the following extremely unrealistic conditions: 1) perfect price and wage-rate elasticity; 2) absence of "money illusion" (orientation upon real instead of nominal values of income, bonds, money balances); 3) absence of a redistributive effect (i.e. changes in the initial distribution of incomes, bonds, and money balances between economic agents as a result of price changes); and 4) inelasticity of expectations concerning future price changes (lack of response to a possible development of inflation). In addition, among the important premises of the model (in the first edition of his work) were the presence in the economy only of unredeemable paper money issued by the government to cover its budget deficit, and the absence of a national debt.

A breach in only one of these "heroic" assumptions (as Modigliani aptly called them) substantially weakens or altogether eliminates the "real balance effect", and Patinkin himself was forced to admit that his conclusions were abstract and unrealistic.[2] So, a switch-off of the flexible prices mechanism, the absence of their elasticity, i.e. the first assumption, eliminated the mainspring setting in motion the revaluation of assets, which serves as

[1] Don Patinkin, *Money, Interest, and Prices*, pp. 651-664.
[2] *Ibid.*, pp. 274-312.

a necessary element in the real balance effect. But in the contemporary monopolised economy of capitalism, a (downward) inelasticity of prices is an incontrovertible fact clearly indicated by postwar statistics in most countries. Furthermore, the introduction of a "money illusion" (Patinkin's second assumption), i.e. orientation upon the nominal value of money indicators, eliminates the "point of reference" to which the behaviour of economic agents is "tied" and worsens or altogether eliminates the "real balance effect". Contrary to Patinkin's constructs, based on the absence of "money illusion", the acts of economic agents in the real conditions of capitalist reproduction are far from always rational. The disruptive effect of inflation on incomes under a relatively slow development of the process is not felt all at once, but with a definite lag, and produces very different responses on the part of individual groups of the population. Being satisfied with the rise in nominal incomes, many economic agents fail to notice the decline in the purchasing power of money. In view of this, some economists believe that Patinkin was justified in his assumption of the absence of "money illusion"[1].

The ignoring of the redistributive effects of price changes is one of the most unrealistic assumptions. Numerous works proved that inflation and deflation do not at all equally affect the various classes and social groups. The first to be hit by inflation are the poorest strata, who lose a sizable part of their incomes, which are appropriated by business firms and the capitalist state. Redistribution processes

[1] E. J. Kane and Alwin K. Klevorick, for instance, assume that a degree of "money illusion" arising from an insufficiently correct evaluation by economic agents of the real value of their assets is inevitably present in the economic process. They think that this markedly weakens, while not altogether eliminating, the "real balance effect". (E. J. Kane, A. K. Klevorick, "Absence of Money Illusion: A Sine Qua Non for Neutral Money?" In: *The Journal of Finance*, September 1964).

occur on a large scale between creditors and borrowers.[1]

Finally, the inelasticity of expectations does away with the uncertainty concerning the future movement of prices. For instance, anticipation of faster inflationary processes in the future could well lead to panic buying of goods and to an even faster growth of prices. Such a response would alter the "habitual" level with which the actual money balances are compared. Stability of this level is seen as a necessary condition for the conclusion concerning the equi-proportional changes in prices. In other words, instability of expectations concerning the price dynamics substantially weakens or eliminates the "real balance effect" altogether. But the anticipation of inflationary price movements is an important process which has increasingly attracted the attention in the recent period.

So, the premises of Patinkin's model turn out to be invalid. But perhaps even more devastating for his conception are the two other assumptions: the existence in the economy only of paper (and not credit) money, and the absence of the national debt.

The evolution of the monetary system of capitalism has produced a situation in which credit money (banknotes and bank deposits) is the most typical and widespread element of the money supply and the chief instrument of the payments turnover. This type of money, being evidence of debt, cannot be referred to "net wealth", and, consequently, does not provide a basis for the emergence of the "real balance effect". The point is that credit money, issued by private banks, simultaneously serves as assets for the non-financial sector and as liabilities for the banks themselves. Changes in the purchasing power of money will have the opposite effect for

[1] See: G. L. Bach, J. B. Stephenson, "Inflation and Redistribution of Wealth". In: *The Review of Economics and Statistics*, February 1974.

creditors and for debtors, the total effect being equal to zero, so that a change in the real value of cash balances consisting of credit money will not alter the aggregate commodity demand in the private sector.

By assuming the existence of one type of money, Patinkin simplified the contemporary monetary system to the utmost, ignoring important features of its institutional structure. It was Gurley and Shaw who first pointed out his mistake when they suggested that money should be divided, depending on the character of the issue, into "inside" money and "outside" money, the former entering the private sector from outside, and the latter emerging within the system through the extension of credit by some economic agents to others.[1] Subsequently, this was broadly accepted by one and all, including Patinkin himself (in the second edition of his work).

One must say that this division of money into "outside" and inside" money is very vague. Where are we, for instance, to include central-bank banknotes? Strictly according to the logic of Gurley and Shaw, these banknotes should be included in "outside" money, as having been issued by the state. But economically, present-day banknotes can also be in the form of paper money, or credit instruments of circulation, depending on the type of transaction which has produced their issue. In present-day conditions, *all* money (even that not determined by the requirements of circulation) is issued through credit channels. That is why the division of money into "outside" and "inside" money fails to meet the truly scientific criterion.

Another source is connected with the characteristic of the national debt. Patinkin neglected it as an element of "net wealth". Other economists disagree, asserting that it is an element of "net wealth", i.e.

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[1] John G. Gurley and Edward S. Shaw, *Money in a Theory of Finance*, the Brookings Institution, Washington, D. C., 1960, Chapter 3.

a basis for the emergence of an effect similar to the "real balance effect"[1]. But in that case, the existence of a national debt in the economy once again invalidates the conclusion concerning an equi-proportional change in money and prices.

Consequently, even in purely theoretical terms, the "real balance effect" and its interpretation in Patinkin's works confront serious difficulties. First, the "basis" for the emergence of this effect in the form of a specific stock of assets ("net wealth") is very narrow. Second, the existence of credit money and the national debt in the economy invalidates one of the chief conclusions concerning the operation of the effect: precise proportionality of the changes in money and prices.

Patinkin's conception and his conclusions in the neoclassical spirit had a great influence on the struggle between the leading trends in bourgeois economics. There emerged in the writings of the 1960s a symbiosis of classical and Keynesian views based on the recognition that the capitalist system was basically stable, the weakness of the "real balance effect" being compensated by the Keynesian programmes for "pumping up" demand. But the sharp worsening of the economic situation in the early 1970s once again drew attention to the disproportionality and instability of the economic development of capitalism.

4. "Money Economy" Doctrine

Money in the theory of exchange. It has already become an axiom that the popularity of Keynesian theoretical analysis in Western economic writings tends to have its own cycles, fluctuating under the impact of the overall changes in the economic

[1] W. Smith, "On Some Current Issues in Monetary Economics: An Interpretation". In: *The Journal of Economic Literature*, September 1970.

situation. With every fresh aggravation of capitalist contradictions, a worsening of the economic situation, and a deepening of class conflicts, bourgeois economists as a rule again turn to the Keynesian theoretical legacy, hoping to find in it the answer to the economic and political cataclysms and recipes for eliminating or easing them. When the outlook is bright, there is, as a rule, a step-up in the campaign against Keynesian doctrine as a specific theory of the "depressive economy", and a sharp swing to the neoclassical interpretation of the capitalist system as a "self-regulating" type of economic organisation which has no need for programmes of government regulation.

These sharp swings from dirigism to advocacy of spontaneous mechanisms—an important specific feature of present-day bourgeois economics—have been most pronounced over the past two decades. The relatively favourable outlook of the 1950s and early 1960s, which led to a revival of neoclassical views and of interest in the neoclassical models of general equilibrium and economic growth gave way by the end of the 1960s to a fresh aggravation of contradictions in the world capitalist economy. The economic stagnation in the late 1960s, with its higher rate of unemployment, lower rate of economic growth, and a foreign-trade and monetary war among the leading capitalist countries, together with the exceptionally rapid inflation once again drove the theory based on "neoclassical synthesis" models into a dead end. The models of general market equilibrium worked out on the basis of the ideas of Walrar and Marshall were once again sharply criticised fos being too abstract and for failing to take into account the specific features of capitalist reproduction, which constantly lead to the emergence of disproportions.

This criticism echoed the class conflicts and upheavals in the capitalist countries that led to the rapid development in bourgeois economics of a radical trend pivoted on criticism of the economic and political institutions of capitalism in contrast to the economics of the bourgeois Establishment.

The actual failure of monetarist recommendations for government economic policy also spread disappointment in neoclassical analysis. Far from stemming the inflation, monetary restrictions in the United States and some other countries sharply intensified the trend towards stagnation and unemployment. President Nixon's 1970 phrase "We are all Keynesians now" symbolised the swing in economic policy from neoclassical recipes, and a new, even though not so obvious, shift in bourgeois economic thinking in the West.

The current debate is still essentially centred on this ideology-based issue: is capitalism a basically stable and viable system, does the capitalist economy have the capacity for spontaneous self-regulation or does its functioning increasingly depend on corrective measures by the government.

The Walras model of general market equilibrium and all its subsequent modifications in the works of Hicks, Modigliani and Patinkin depict the capitalist economy as a coherent system in which transition from one state of equilibrium to another proceeds painlessly and virtually instantaneously. This coordination is achieved through a special procedure, namely, the discovery of the vector of relative equilibrium prices (exchange proportions) on all the markets before the start of exchange, which ensures total correspondence of demand and supply, and accordingly, a complete "clearing" of goods from every market. Walras designated this process as "atonement", and Edgeworth as "renegotiation of contracts". Subsequent models of general equilibrium also use some form of a similar apparatus for internal regulation of the system.

Thus, provision is made for the presence in the economy of some kind of "supreme coordinator" (or "auctioneer", as Walras called it), who processes all the vast market information and "appoints" equilibrium prices ensuring the coordinated operation of the separate economic agents, with the result that on the scale of the whole economy demand is equal to supply, in other words, the total amount of excessive demand on all the markets is equal to zero. This has been designated as the "Walras Law".

The apologetic thrust of this theoretical construct is obvious, for it idealises the capitalist mode of production and depicts the anarchic capitalist economy as a harmonious and coherent system in which the acts of millions of economic agents are allegedly precisely coordinated, in which the prospects are clear and the results predictable. In this theoretical construct, all manner of disruptions and disproportions appear as extraneous and accidental phenomena, as deviations from the tendency to stable growth.

Actually, as soon as bourgeois economists get down to analysing real economic situations, they at once have to face the incontrovertible truth that equilibrium is only an accidental and transient moment in the process of capitalist reproduction. Keynes himself was forced to admit that instability is a typical feature of capitalist development. But this side of his analysis—emphasis on the internal instability of the capitalist economy—was smoothed over and neutralised in the conception of "neoclassical synthesis".

The neo-Keynesians opposing the neoclassical doctrine seek to lead economic theory out of the impasse created in economic models by the presence of a mythical "supreme coordinator". The activity of the whole complex of economic agents in a haphazard market situation and essentially decentralised economic decision-making cannot be coordinated in advance in a planless economy, where the main goal is maximisation of profits and where the vector of equilibrium prices is not known in advance to the economic agents. The absence of the necessary proportions and equilibrium prices is, in fact, an economic reality, and this is most explicit when it comes to evaluating and predicting future trends in economic growth. The acts of capitalist firms and consumers are forcibly regulated in the course of the economic process itself, so that equilibrium is ultimately enforced, with the economic losses of such "coordination" being exceptionally large.[1]

Some other bourgeois economists agree with this.

There is a growing awareness among Western analysts that the hitherto widespread abstract models of general market equilibrium cannot be used to study economic situations which are anywhere close to the reality. There is a growing understanding among a section of bourgeois economists that if economic science sets itself the goal of moving closer to the actual state of things there is a need to study the disturbances of the state of equilibrium and the response of economic agents to these disturbances, rather than equilibrium in the conditions of steady-state growth. Indeed, it is the practical

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[1] Paul Davidson, who had joined the neo-Keynesians in attacking the idealised notions of the capitalist mechanism of reproduction, writes: "In the real world, booms and slumps are not merely erratic episodes which can be readily superimposed onto long-run steady-state growth path of an economy. The actual historical path of economic activity for real world monetary economics is not one which can be decomposed into separate and logically independent secular trend and short-run trade cycle aspects. (Such a dichotomous construction is merely the handiwork of the economist's imagination...). Any theoretical model which is logically applicable only to an economy which is in long-run equilibrium or steady-state growth may be a useful 'warming up' exercise for the muscles of scientific inquiring minds, but it should never be taken as a serious description of a real world alternative, and no reliance as either a predictor or as a basis of policy can be given to such callisthenics where money is concerned." Davidson goes on to say that models in which all changes can be foreseen from the beginning, so that coordination of actions is possible, "represent retrograde rather than progressive developments in monetary theory" (Paul Davidson, *Money and the Real World*, Macmillan, London, 1972, pp. 8-9).

uselessness of the general equilibrium models that is the main reason for the current revival of interest in Keynes among bourgeois economists.

The calls for a "return to Keynes" inevitably lead to emphasis on the role of money as the main economic institution which, according to Keynes, is the embodiment of the erratic factor, one that introduces elements of inorganisation, risk and "unforeseeable future". There is a good reason for the return to Keynes's conception of "money economy". Bourgeois economists now regard the specifics of money exchange, with its inherent fragmentation of purchase and sale into two independent acts as an expression of anarchy and uncoordination of the economic system which produces disproportions and upsets "smooth" development.

The campaign for a "rehabilitation of Keynes" and a return to his "original" ideas was started by two articles by the US economist R. W. Clower concerning the specifics of money exchange and the treatment of money in general equilibrium models.[1] This was followed by A. Leijonhufvud's book with a reappraisal of some Keynesian ideas that drew rapturous reviews in the Western press.[2]

Although these works are seen as an explanation and interpretation of Keynes's ideas, their authors' conception is substantially different from his, for they have most frequently to consider what Keynes actually "meant to say", and what he "had in mind".

The "money economy" theory emerged from the consistent criticism of the version of neoclassical doctrine which Clower calls the "neo-Walras theory

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[1] R. W. Clower, "The Keynesian Counterrevolution: A Theoretical Appraisal". In: *The Theory of Interest Rates*, Ed. by F. H. Hahn and F.P.R. Brechling, London, Macmillan & Co., 1965, pp. 103-125; also his, "A Reconsideration of the Microfoundations of Monetary Theory". In: *Western Economic Journal*, Vol. 6, March 1967, pp. 1-9.

[2] Axel Leijonhufvud, *On Keynesian Economics and the Economics of Keynes*, Oxford University Press, New York, 1968.

of money and prices". This conception is based on the above-mentioned Walras Law. The advocates of the new version of Keynesian doctrine hold that this law, reflecting the conditions for a general equilibrium of all markets, is applicable only in a barter economy, so that the logic of the law becomes meaningless with the introduction of money into the model.

The Walras Law (on the clearing of all markets under a general equilibrium) is based on the unrealistic assumption that the supply of any commodity finds adequate demand, and in this sense all commodities have absolute liquidity. In other words, demand is boundless, so that all the commodities offered on the market can be exchanged for other commodities without hindrance. Strictly speaking, this is a detailed expression of the central idea of Say's theory of realisation: supply produces demand. But it is quite obvious that the equality of supply and demand in these models can be achieved only through a preliminary coordination of the plans and intentions of all the economic agents, something that is impossible in the erratic capitalist economy. The role of coordinator is assumed by a mythical "auctioneer", who conveys to all the participants in the exchange the vector of equilibrium prices.

In Walras-type models, money is a purely external and formal element, and is regarded as an ordinary commodity which may or may not be involved in exchange. That is the basis for Clower's refutation of such models, for in the actual market situation the typical transaction entails the exchange of a commodity not for some other commodity but only for a definite commodity, for money. Accordingly, in order to buy any commodity one must have a stock of money. This imposes special limitations on the behaviour of economic agents and complexifies their acts.

Furthermore, the accent on the formal aspects of exchange in a barter and a money economy provided the basis for the equally abstract theory of "disequilibrium situations", in which the difficulties of reproduction are straightforwardly deduced from the difficulties of the exchange process itself. Present-day interpreters of Keynes see his main merit in the abandonment of a "supreme coordinator" conveying equilibrium prices. This is a peculiar form of recognition of the anarchic nature of capitalist reproduction. What would happen, they ask, if one were to eliminate the coordination of the acts of economic agents by means of an externally given price vector which ensures the total clearance of the market? In that case, the exchange would run over a more or less lengthy period of time at non-optimal ("false", says Hicks) prices. The outcome will be underemployment.

The neoclassics started from a very rapid adaptation of economic agents to the new market conditions. In the Keynesian model, the response on the part of economic agents to the new prices is slowed down. There is considerable inertia caused by the ignorance of future trends in economic development. The economic agents regard a price level which existed for a long period as a "normal" or "stable" one and at first believe that the change in prices is a temporary deviation from that level. That is why with the change in prices many economic agents refrain from operations and begin to seek more profitable offers, in the hope that prices will soon return to their old level.

But, the neo-Keynesians say, such hitches in the process of exchange, when these spread to all the commodity markets, produce a chain reaction that has an extremely unfavourable effect on the economic system. If an economic agent in possession of a commodity temporarily refrains from selling it at the changed (disequilibrium) prices in search of more profitable terms, his stock of money, the "universal commodity", declines, the demand for other goods declines accordingly. This produces a chain reaction: if a commodity is not realised (not sold for money), the effects of this will be felt not only on the market of the given commodity, but on other markets as well, for this means that somewhere in the economy there is an accumulation of money that is required to ensure effective demand for other commodities.

According to the "money economy" theory, the "unemployment" of resources (including the commodity labour power) arises from a mutual dovetailing and dependence of transactions in the money economy. In the absence of "correct" (equilibrium) prices, there is a search for new exchange proportions which may last for a long time and which narrows down the potentialities for commodity realisation. There arises a chain reaction of a general reduction of demand, which is based not only on prices but also on the regular influx of money incomes in the course of the period. Exchange at disequilibrium prices results in a "discoordination" of the system, the emergence of a chain reaction of commodity accumulation among sellers and money among buyers, and ultimately in production cutbacks.

One could draw the conclusion that on the whole the contemporary bourgeois theory of money is an arena of sharp clashes between different trends. The battles being fought over various aspects of government regulation of the economy testify to the confusion in the ruling circles of the capitalist countries in face of the sharpening contradictions of capitalism.

The problems which are now of concern to bourgeois economists were scientifically solved by Marx over a century ago in his *Contribution to a Critique of Political Economy* and *Capital*. Marx gave a dialectical analysis of the contradictions of commodity based on the two-fold nature of the labour it contains. Money resolves the inner contradictions of exchange by providing the commodity world with a form of universal embodiment of value, a crystallisation of abstract labour.

This dichotomy of the act of purchase and sale produces a mechanism of spontaneous accounting and regulation of labour inputs in the economy on the basis of the law of value: surplus commodities cannot be sold for money at the existing prices, and this signals the need for a restructuring of production, a redistribution of labour and capital between the industries, etc.

At the same time, Marx emphasised that the emergence of money from the world of commodities produces only a *nominal* possibility of crises. If this possibility is to be fully realised, there is a need for a developed system of capitalist relations of production, which hourly and inevitably generate a general discoordination of the economy, periodical shortages (or surpluses) of effective demand, and so on.

More than a century after Marx, bourgeois economists are still debating the theoretical problems which mark the start of a scientific analysis of the contradictions of commodity exchange and their effects under capitalism. Their studies, including the works of the neo-Keynesians, at best merely give a glimpse of the obstacles with which present-day capitalist reproduction is constantly confronted, but they cannot show the real objective causes for the constantly emerging disproportions.

CHAPTER FOUR

THE PROBLEM OF INFLATION

Inflation, now the central problem of all social life in the capitalist countries, has also been looming ever larger in economic theory. Let us note that the various schools making up the vast and disordered area of economic theory[1] have not even tried to produce a uniform notion of inflation. Thus, the Swedish economist Bent Hansen says there are twelve, the Frenchman P. Biacabe 32, and the West German F. Läge 60 "types of inflation" or different uses of the term in economic writings.[2] Accordingly, some bourgeois economists want to "ban the term and the notion of inflation both from the economic lexicon and from the current language".[3] But most frequently a different approach is preferred: the term "inflation" is used with various attributes de-

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[1] A. Brown, "Review on B. Hansen". In: *Economica*, February 1955, p. 81.

[2] B. Hansen, *A Study in the Theory of Inflation*, George Allen & Unwin, New York, 1951, p. 27; P. Biacabe, *Analyse contemporaine de l'inflation*, Sirey, Paris, 1952, p. 1; F. Läge, *Die Säkulare Inflation*, Frankfort on the Main, 1959, p. 33.

[3] Georges Manoussos, *Inflation croissance et planification*, Librairie E. Droz, Geneve; Librairie Minard, Paris, 1961, p. 317.

signed to help the reader understand the kind of inflation the author has in mind.[1]

In order to gain a better understanding of this theoretical discord on one of the key phenomena of contemporary capitalism, let us consider, first of all, the preceding development of economic theory.

Smith and Ricardo, the classics of political economy, saw the movement of commodity prices as being above all connected with changes in the labour inputs into the production of the given commodities, and also with changes in the value of full-value money. But they also saw a clear distinction between the movement of prices and the movement of values. A year before the publication of his chief work, *The Principles of Political Economy and Taxation*, Ricardo said that commodity prices could move in a direction opposite to the movement of value; for instance: "The price of a commodity may rise while its value falls, and *vice versa*."[2] Still, neither Smith nor Ricardo succeeded in deducing the form of value from their analysis of commodities. Karl Marx said that one of the basic failings of classical political economy was the fact that it had never succeeded from the analysis of commodities, notably, from commodity value, to derive the form of value, which is precisely what makes it an exchange value.[3] But the whole point is that the analysis of the form of value and exchange

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[1] One no longer speaks of simply inflation nowadays, according to the US economist W. Bowen. One has to specify the kind of inflation one means: cost-push, demand-pull, excess-demand, wage, money, structural, cumulative, sellers' inflation, buyers' inflation, overpricing inflation, fixed-price inflation, etc. (W. Bowen, "'Cost Inflation' Versus 'Demand Inflation': a Useful Distinction?" In: *Southern Economic Journal*, January 1960, p. 199.)

[2] *The Works of David Ricardo*, by J. R. McCulloch, John Murray, London, 1846, p. 401.

[3] Karl Marx, *Capital*, Vol. I, Progress Publishers, Moscow, 1974, p. 85.

value is especially important for analysing the changes in the general level of commodity prices and the purchasing power of money.

The development of this trend in the subsequent period inevitably brought to the fore, in non-Marxist economic theory, an analysis of the correlation between commodity prices; in such theoretical schemes, the level of the relative prices taking shape depended only on "real" factors. That is why when tackling the problem of price formation one could, according to John Stuart Mill, simply ignore things like the quantity of money in circulation and the purchasing power of the money unit.[1]

The development of the concepts of subjective utility completely eroded the theoretical divide between value and price.[2] The correlation between the marginal utilities of two commodities, which determine the subjective assessments of their value, inevitably appear, under market equilibrium, as proportions between their prices. This centres analysis on the exchange values of commodities, on the proportions in which one commodity is exchanged for another. However, changes in these proportions (relative prices) say nothing at all about the change in the absolute level of commodity prices.

This produced a situation in which microeconomic theory, which was something of a backbone for the turn-of-the-century political economy, assigned only a secondary role to changes in the general level of prices. Thus, the price theory resting on the principle of partial equilibrium (A. Marshall), and

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[1] See: John Stuart Mill, *Principles of Political Economy*, Longmans, Green and Co., London etc., 1926, p. 488.

[2] An early theorist of subjective utility, Etienne Condillac, saw price as a relation of subjective assessments of the value of two commodities being exchanged. It followed that such assessments of value and price were, essentially, completely synonymous (E. Condillac, "Le commerce et le gouvernement". In: *Mèlanges d'économie politique*, Vol. 1, Paris, 1847, pp. 25-26).

general equilibrium models (Walras), concentrated on price structure alone.[1]

Since Pareto's time, equilibrium models have explicitly or implicitly used the assumption that the key proportions are characterised by a zero-degree homogeneity for prices.[2]

That approach has been extremely static from the outset, so that when analysing the movement of prices, many theorists compared it with the ordinary swings of the pendulum.[3] Within the framework of such notions it is, in effect, impossible to solve the problem of why, after all, there is a constant movement from one absolute price level to another. It turns out, Robert Lekachman remarked, that

> "in one of his roles, the economist frequently insists on the progressive character of capitalism; in another, he carefully empties most of the change out of his categories."[4]

That is why the consideration of inflation, as a theoretical problem in its own right, reveals the deeply contradictory nature of traditional neoclassical schemes. When, at the turn of the century, the question of rising prices came to be broadly debated in economic writings in view of the general growth in the cost of living, L. von Mises, one of the best-known theorists of the period, had to declare

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[1] Analysing general equilibrium systems, Hansen said that orthodox economic theory has never given a satisfactory answer to the question of "what is it, exactly, that determines the rate at which a price will change?" (Bent Hansen, *A Survey of General Equilibrium Systems*, McGraw-Hill Book Company, New York etc., 1970, p. 119.)

[2] A k-degree homogeneous function is one for which any value of m will satisfy the condition $f(mx_1, mx_2, \ldots mx_n = m^k f(x_1, x_2, \ldots, x_n)$.

[3] See: W. Jevons, *The Theory of Political Economy*, Macmillan and Co., London, 1924, pp. 93-94; A. Marshall, *Principles of Economics*, Macmillan, London, 1920, p. 345.

[4] Robert Lekachman, *A History of Economic Ideas*, Harper & Brothers Publishers, New York, 1959, p. 383.

that the "forty-year development of the theory of subjective utility has left virtually no trace at all."[1]

The "classical dichotomy" implied that transition to new conditions in the production of all commodities (except money), like the changes in demand on the individual commodity markets merely entail changes in the structure of relative prices, while the movement of absolute prices could be connected only with changes in the scale of money circulation. General equilibrium models gave a one-sided interpretation of the function of money: it is, after all, not very hard to include the equations of money supply and demand into the system of Walras's equations, but in such a model the relations between money and commodities are virtually indistinguishable from barter exchange.

Thus, it is very hard to deduce from orthodox microeconomic theory, from the postulates characterising the behaviour of consumers and businessmen, the trend towards the steady rise in the general level of prices.[2] Within the framework of these assumptions, the steady development of inflation, which tends to accelerate in some periods, can be connected only with the special mode of functioning of the monetary sector of the economy. This paved the way for theoretical notions about inflation being simply one of the consequences of changes in money supply.

1. The Monetarist Concept

The monetarists believe that short-term price changes can be caused by various factors, but that protracted inflation is always and everywhere

[1] *Archiv für Sozialwissenschaft*, 1913, Book 3.

[2] Kenneth Arrow quite rightly remarks: "The weakness in inflation theory goes right down to the microlevel, to the theory of price determination at the level of the individual firm" (*Business Week*, June 29, 1974, No. 2337, p. 59.)

a purely monetary phenomenon. Milton Friedman says that inflation can occur only when the quantity of money increases faster than the quantity of the product.[1] The behaviour of prices over the more or less lengthy period, according to the monetarists, should be fairly flexible.[2] The tendency of prices to rise is evidence of an "excessive" expansion of the aggregate money supply, which is why surplus money supply should always be regarded as the only and immediate cause of inflation.[3]

Friedman and other members of this school have carried out extensive statistical calculations to show that any increase in money supply in excess of the GNP growth rate inevitably leads to a general rise in prices. That is why throughout the whole history of the United States and other capitalist countries the growth of money stock in circulation supply has been the only motive force of inflation. Friedman rejects the other conceptions and believes that purely monetarist considerations can explain the growth of prices over a period of nearly two centuries, so that these could provide an adequate explanation of the inflation that has gathered momentum in the recent period.[4]

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[1] Milton Friedman, "The Counter-Revolution in Monetary Theory". In: *IEA Occasional Paper No. 33*, London, 1970, p. 24.

[2] Whenever the monetarists have to admit that price responses are insufficiently flexible, they are inclined to regard this merely as resulting from the unwarranted intervention by trade unions and the government into the free functioning of the market syste .

[3] The well-known French economist Jacques Rueff says that "there can be no inflation without the existence of surplus cash, and no surplus cash without inflation". ("The Control of Inflation by Monetary and Credit Policy". In: *Inflation*, Proceedings of a Conference held by the International Economic Association, Ed. by D. C. Hague, London, Macmillan and Co., Ltd., 1962, p. 165).

[4] *Industrial Relations Research Association. Proceedings of 11th Annual Meeting*, New York, 1958, pp. 212-213.

Earlier versions of the quantity theory of money were most frequently based on the assumption that over not too lengthy periods of time monetary velocity tended to remain more or less constant, so that the general level of prices had to rise in the same proportion as the expansion of money supply. Today, the monetarist view of inflation is most frequently based on somewhat modified premises of the quantity theory of money. It allows that monetary velocity in certain conditions, say, in the conditions of rapid, "galloping" inflation, may change, and says that such changes are one of the key aspects of the inflationary process. But according to the monetarists, it is always possible to single out the function connecting demand for real money balances with several independent variables, including income level, a function that is especially stable. When money supply changes, nominal income should change in such a way as to re-establish equilibrium proportions between the demand for money and income.

Throughout the postwar period, there has been a trend towards a long-term increase in the indicators of monetary velocity (especially indicators calculated for the M_1 aggregate). Such growth, which occurs under intensive inflation, has once again emphasised the importance of the correlation between the movement of indicators characterising aggregate output, and the turnover of commodities and financial assets, on the one hand, and money supply, on the other. Economic statistical studies have shown that Keynes's "basic law of consumption" is untenable, and that the properties of the elementary Keynesian-type consumer functions are unsatisfactory.

In the new conditions, the monetarists prefer to take a more flexible approach, and although some Western economists and official government documents frequently assert that monetary velocity remains constant over fairly long periods, there has still been a gradual shift of emphasis in theoretical constructs: stability of monetary velocity is now being derived from the stability of relations between that indicator and other parameters of economic development, most frequently with the stable part of aggregate personal income and/or with the cost of keeping money. Friedman says:

> "There is an extraordinary empirical stability and regularity to such magnitudes as income velocity that cannot but impress anyone who works extensively with monetary data."[1]

In the early 1960s, Friedman and Meiselman announced that they were offering, for the first time, the solution of the problem on the strength of concrete statistical data: "The question at issue is mainly the short-term stability of the relations being compared."[2] After a series of regression calculations, they reached the following conclusion: the relations in which monetary velocity is used have invariably turned out to be more stable over short-term periods, than, say, the Keynesian models describing the acceleration effect of "autonomous" investments. This, according to Friedman and Meiselman, proves the superiority of the monetarist models, in which money supply is held to be the main source of movement in the economic system, over the Keynesian models, in which the dynamics of production and prices is set by "autonomous" investments. This sparked off a long discussion among Western economists.[3]

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[1] Milton Friedman, "The Quantity Theory of Money—A Restatement". In: *Studies in the Quantity Theory of Money*, p. 21.

[2] Milton Friedman, David Meiselman, "The Relative Stability of Monetary Velocity and the Investment Multiplier in the United States, 1897-1958". In: *Stabilisation Policies*, Englewood Cliffs, 1963, p. 174.

[3] D. Hester, "Keynes and the Quantity Theory: A Comment on the Friedman-Meiselman CMC Paper". In: *The Review of Economics and Statistics*, Vol. XLVI, November

From the standpoint of monetarism, the post-war rise in prices has ultimately been caused by expansionist monetary and credit policy and, consequently, the blame for this falls mainly on the management of the bank of issue. Friedman gives this popular explanation:

> "the inflation is made in Washington, in that stately and impressive Grecian temple on Constitution Avenue that houses the Board of Governors of the Federal Reserve System."[1]

The monetarists have not given any detailed description of the mechanism by means of which inflation develops, and most frequently use the "black box approach". In the most general terms, this mechanism could apparently be described as follows:

It is usually an increase in the money stock that serves as the initial impulse to inflation. Excessive expansion of money circulation means that cash balances at the disposal of business and consumers (money supply) are in excess of real requirements (money demand). In that case, after some time (roughly within 6 to 9 months, according to Friedman) the rate of nominal income growth will increase, and with it the growth of the nominal GNP, because owners will want to get rid of the "surplus"—under the given price level—money balances, so increasing their spending. Nowadays, the monetarists are prepared to admit that the

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1964, No. 4; Albert Ando, Franko Modigliani, "The Relative Stability of Monetary Velocity and the Investment Multiplier", M.De Prano, T. Mayer, "Tests of the Relative Importance of Autonomous Expenditures and Money". In: *The American Economic Review*, Vol. LV, September 1965, No. 4; William Poole, Elinda B. F. Kornblith, "The Friedman-Meiselman CMC Paper: New Evidence on an Old Controversy". In: *The American Economic Review*, Vol. LXIII, December 1973, No. 5, pp. 908-917.

[1] Milton Friedman, "The Inflationary Fed". In: *Newsweek*, Vol. 73, No. 3, January 20, 1969, p. 46.

immediate response of the market to an expansion of money demand is not a transition to new and higher prices, but a growth of supply as a result of some reduction in inventories and, chiefly, an increase in output.[1]

The following stage of the process comes some eighteen months after the trend towards a growth of output has set in. By then, the market assessments and expectations of economic agents have changed, so that the growth of output gives way to a rise in the general level of prices.

The growing cost of living, for its part, inevitably reduces the real purchasing power of money balances, so increasing the economic agents' cash requirements. This process will continue until the amount of payments instruments in circulation becomes equal to the demand for ready money on the part of business and consumers. The advance to a new point of equilibrium can be ensured only as a result of the general price level. Such models as a rule fail to examine the structural and dynamic aspects of the problem.

But, however that may be, the monetarists believe that the inflationary process (as, incidentally, the more general mechanism of cyclical expansion

[1] This interpretation of the response of the economic system to an expansion of aggregate money demand is noteworthy. In one of his works (*Essays in Positive Economics*, The University of Chicago Press, Chicago, 1953, pp. 41-42), Friedman says that existing relative price theory reached almost its present form in Marshall's *Principles of Economics*. However, Marshall and his followers assumed that expansion of money demand leads over a short term to a rise in prices and only later, to an expansion of market supply. However, apparently in the light of the development of the capitalist economy over the past two decades, Friedman and other monetarists have had to abandon the traditional neoclassical notions of an instant price response to the existing relations between market demand and supply. Monetarist schemes assumed the opposite sequence (output was the first to respond to an expansion of money demand), while the behaviour of prices appeared to be flexible only over a longer period.

and reduction of output[1]) is based on changes in money supply and demand for money on the part of the population. Thus, if the old ("rough") version of the quantity theory of money formulated only the correlation which had to be established over a more or less lengthy period, the new ("modern") version claims to do more: it undertakes to explain the short-term fluctuations in economic activity, and transient price movements.

In accordance with monetarist assertions, the growing money supply should be accompanied with a growth in the nominal money income. This growth may result both from an expansion of output and a rise in prices. In this way, the short-term effects of the money impulse appear to be split between nominal magnitudes (a change in the price scale) and real economic proportions (including relative prices), so bringing out the inadequacy of elementary monetarist constructs.

In order to find a way out of this difficulty, without jeopardising the idea of the crucial role of the monetary factor, some Western economists suggest a distinction between the impact of a growth in the absolute money supply, and the velocity, rather, the accelerations (or decelerations) in the movement of the total of monetary instruments. Karl Brunner, one of the most influential spokesmen for the "new monetarism", says:

> "The pressure of monetary growth is dominantly on the price level. Monetary accelerations (or decelerations), on the other hand, dominantly influence the pace of economic activity."[2]

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[1] Don Patinkin, "The Chicago Tradition, the Quantity Theory and Friedman". In: *The Journal of Money, Credit and Banking*, February 1969.

[2] Karl Brunner, "The Monetarist View of Keynesian Ideas". In *Lloyds Bank Review*, October 1971, No. 102, p. 39.

This implies that both the economic activity and the level of prices, crucially depend on changes in money supply.[1]

Much importance in contemporary monetarist schemes is attached to a distinction between expected and unexpected inflation. Only unexpected changes in money supply—a role usually assigned to the acceleration or deceleration in the growth of money supply—can have an influence on short-term changes in real economic processes (and also on the rate of growth of the general price level). Elementary adaptive processes are, as a rule, used to describe the shaping of expectations.[2] However, the monetarists most frequently lose sight of the concrete channels and economic forms through which these expectations exert an influence on the movement of incomes, prices, and rates of interest.

These theoretical principles are visually embodied in monetarist econometric models, which were

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[1] Let us note that some economists, following Fisher, have accented the impact of monetary impulses on the shaping of the relative prices of real and financial assets, and on the movement of interest rates (Brunner called this approach to the "transmission mechanism" a weak monetarist approach. (See: K. Brunner, "The Role of Money and Monetary Policy". In: *Federal Reserve Bank of St. Louis Review*, Vol. 50, July 1968, pp. 9-24). But it is the stronger approaches that mostly come to the fore in the analysis of the mechanism of inflation.

[2] Thus, in an article entitled "A Monetary Theory of Nominal Income" (*The Journal of Political Economy*, March-April 1971) Friedman uses these equations:

$$\frac{dY_t}{dt}\left(\frac{dY_t^*}{dt}\right)=\left(\frac{dY_t}{dt}-\frac{dY^*}{dt}t\right),$$

where Yt is the actual nominal income at point t, and Y^* is the expected nominal income at the same point, and the parameter characterising the speed at which expectations adapt. A similar process of expectation formation was earlier described in Phillip Cagan's model of hyperinflation. (See: Ph. Cagan, "The Monetary Dynamics of Hyperinflation". In: *Studies in the Quantity Theory of Money*, Ed. by M. Fiedman, The University of Chicago Press, Chicago, 1956, pp. 25-117.)

most widely accepted in the late 1960s and early 1970s.[1] These models were produced for analysing short-term changes in GNP and its components, but they also included equations describing the behaviour of prices. In such equations, the number of independent variables has as a rule been relatively small, including the variable of money supply (in nominal terms)—current and gross magnitudes—and also some characteristics of economic expectations, including price expectations. These equations are usually recursive. In contrast to other econometric models (Wharton, FRS—MIT—Penn, and others) in which the inflationary growth of prices is deduced from the operation of numerous factors both on the side of money demand and commodity supply, in monetarist models it is the growing money supply that always turns out to be the only cause of the steady growth of prices, with the rise in the general price level roughly corresponding to the additional increase in money supply. Consider the calculations for the Andersen-Karnosky model relating to the 1964-1973 period. The advance in the growth of money supply from 3 per cent to 6 per cent a year must entail an additional price growth of 2.3 per cent a year.[2]

When considering the monetarist conception, one should right away emphasise its key methodological feature: it derives the movement in the general level of prices directly from the interaction of

[1] See, for instance, L. Andersen, K. Carlson, "A Monetarist Model for Economic Stabilisation". In: *Review of Federal Reserve Bank of St. Louis*, April 1970, pp. 7-25; D. Karnosky, "The Link Between Money and Prices—1971-1976". In: *Review of Federal Reserve Bank of St. Louis*, June 1976, pp. 17-23. The critical analysis of the technical methods used by Andersen and Carlson will be found in W. Nordhaus, "Recent Developments in Price Dynamics". In: *The Econometrics of Price Determination*, Washington, 1972, pp. 43-44.

[2] See: L. Andersen, D. Karnosky, "A Monetary Interpretation of Inflation". In: *Analysis of Inflation 1965-1974*, Cambridge Massachusetts, 1977, pp. 22-25.

commodities and money in the process of circulation. It regards the causal nexus in the light in which it appears on the surface of phenomena: it is always an increase in the quantity of money in circulation that is the ultimate cause of the rise in prices. This totally ignores the fundamental economic processes connecting price movements with the value of commodities and money, and so with the processes going on in the sphere of production. But the fact is that the basis of the value relations is shaped in the process of social production, with money merely realising the prices of commodities in the course of circulation.

The external connection between changes in the mass of instruments of circulation and price movements becomes especially obvious when money supply is sharply expanded. There was good reason why the growth in the number of coins in Western Europe following the great geographical discoveries and the working of American mines constituted the "historical background" for David Hume's quantity theory of money.[1]

The specific proportions between the state of money supply and the movement of commodity prices took shape after the collapse of the gold standard. Conditions are now being created for the emergence of an especially protracted and stable break between the movement of the value of commodities and their prices: the growing efficiency in the use of material and labour resources leads to a reduction in per-unit inputs, while the prices of commodities, expressed in paper money, tend rapidly to grow with an inflationary expansion of money supply. All of this has helped to spread the idea that a change in the money supply is the only active force governing the movement of commodity prices.

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[1] Karl Marx, *A Contribution to the Critique of Political Economy*, Progress Publishers, Moscow, 1970, p. 160.

This specific development of economic relations, engendered by the new price formation conditions, has helped to keep monetarist notions very much alive. But when analysing the problem of inflation, the monetarists quite rightly draw attention to the growing deficits of government budgets, the intensive monetary and credit expansion, and, in a number of countries, to the disequilibrium situations taking shape in the sphere of exchange rates.

The rapid growth of money circulation, the sharpening problem of inflation and the painful restructuring of the monetary system, for their part, increase the interest in the role which money now has to play in the capitalist economy.[1] The latter circumstance has largely helped to enhance the influence of monetarism over the past two decades: after all, the monetarists have tried hard to bring out the important role of money in the inflationary process.

Having brought out in the intricate mechanism of inflation a truly important process (over a long term, the growth of money supply, as a rule, is a necessary condition for an especially marked rise in the general price level), the monetarists set it up as a closed and self-sufficient process, leaving in the background the much more fundamental dependence of money supply and demand on the general course of economic development, the succession of phases in the industrial cycle, the nature of technical progress, etc. Or, to use more technical terms, they confine themselves to a consideration of money as an exogenic variable, without discussing the more general systems in which

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[1] Milton Friedman writes: "Double-digit inflation and double-digit interest rates, not the elegance of theoretical reasoning or the overwhelming persuasiveness of serried masses of statistics massaged through modern computers explain the rediscovery of money". (*The American Economic Review*, Vol. LXV, May 1975, No. 2, p. 176.)

money plays the part of one of the endogenic magnitudes. For that reason, the monetarist scheme conveys no information about the other sources of rising prices, which play such an important role in the mechanism of contemporary inflation. There has of late been growing criticism of this superficial and one-sided monetarist approach.[1]

Inflation has never actually been a purely monetary phenomenon, always expressing much deeper economic processes and trends characterising the development of the whole system of social production, distribution, and circulation. Of course, a long-term growth of prices implies a parallel increase in the relation between money supply and physical aggregate product, but it does not at all follow from this that the expanding money supply must always be the crucial cause of inflation.[2] In some instances the growing money supply is itself caused by preceding or parallel (simultaneous) price rises. In the capitalist economy one will now frequently find situations where the initial impulse to price rises has come from "autonomous" regulation by big corporations of the demand-supply relation taking shape on individual commodity markets, and the policy of government regulation (or fixing) of prices.

On the other hand, the monetarists underestimate—however paradoxical that may sound—the

[1] Hicks says that problems facing Western economics today are much too complicated, and that the monetarist prescriptions are inadequate for their solution. (J. Hicks, "The Permissive Economy 'Crisis '75'". In: *IEA Occasional Paper No. 43*, London, 1975, p. 17.)

[2] Analysing long-term trends in the movement of commodity prices, Anna Schwartz makes the assumption that the "secular" increase in prices has been due entirely to excessive money supply. She ends with the following words: "The scatter suggests to me that the key to understanding secular price change now as in the past is the behaviour of money stock per unit of output". (Anna J. Schwartz, "Secular Price Change in Historical Perspective". In: *The Journal of Money, Credit and Banking*, Vol. V, Part II, No. 1, February 1973, p. 267.)

role of money relations and monetary and credit policy in the functioning of the real sector of the economic mechanism. After all, according to their basic postulates, changes in money circulation can cause only some departures from the equilibrium trajectory, but cannot influence the long-term rate of real economic growth. In other words, no monetary and credit policy can over a more or less long period promote the more intensive expansion of aggregate supply (in real terms) through, say, a rise in the average loading of production capacities and a reduction in the number of unemployed. Moreover, the most consistent advocates of this view assume that whatever money and credit policy instruments are used, these cannot even counter the "shifts in the real sector of the economy", like the oil crisis or a sharpening of the situation on agricultural markets. The most curious thing of all is that such assertions usually stem from the blind apologetic faith in the optimal nature of private economic regulation, the faith that over a long term the functioning of the private sector should of itself ensure the most efficient use of material and labour resources. What is more, the current version of the monetarist conception including the hypothesis of rational expectations (these and their role in backing up Friedman's ideas are considered in greater detail below) implies that information concerning subsequent measures in the sphere of government policy has been fully taken into account in advance by all the economic agents, which is why such measures cannot exert an influence on the real scale of aggregate market supply.[1]

Statistical and economic analysis shows that

[1] One economist concludes an article by saying that his approach allows the conclusion that monetary policy has no part in resisting such real shifts (R. Barro, "Rational Expectations and the Role of Monetary Policy". In: *Journal of Monetary Economics*, January 1976).

over the past several decades, monetary velocity has undergone intensive fluctuations connected with the cyclical character of capitalist reproduction, the state of the money markets, monetary and credit policy, etc.[1] This can alter substantially the proportions in the movement of money supply and commodity prices. The remarkable thing is that the US economist Phillip Cagan, one of Friedman's best-known disciples and followers, considering statistical series ranging over almost a half-century, had to reach the conclusion that in the course of short intervals of time one could establish a fairly clear connection between changes in the stock of money circulation and price movements only in a few cases.[2]

Concerning the models of Friedman-Meiselman and their followers—models designed to prove the relative stability of monetary velocity—one has to note that the abridged (discounted) form of the equations they use allows for the most diverse theoretical interpretations of the results obtained. Such equations cannot provide any information about the economic mechanism regulating the stability of monetary velocity; that is why all the judgements concerning the behaviour of this indicator are, to some extent, mysterious. Besides, the conclusion that monetary velocity is more stable than, say, the multiplier of autonomous investment crucially depends on the initial definition of "autonomous" inputs. One need do no more than slightly modify the method for calculating these inputs to obtain models in which the ratio between personal consumption and autonomous investment turns out to be more stable.

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[1] Jan Tinbergen, "Economic Models for the Explanation of Inflation". In: *Stabile Preise in Wachsender Wirtschaft. Das Inflationsproblem*, Tübingen, 1960, pp. 117-118.

[2] Phillip Cagan, *Determinants and Effects of Changes in the Stock of Money. 1875-1960*, National Bureau of Economic Research, New York, 1965, Destributed by Columbia University Press, New York and London.

The modelling of relations which are so poor in economic content is ambivalent, and allows for different interpretations.[1] Empirical verification of the stability of these proportions cannot provide a simple solution of the problem until fuller and clearer characteristics of the analysed economic processes are introduced.

The discussed macroeconomic models based on monetarist (as well as Keynesian) theory invariably revealed their unsatisfactory prognostication properties. The changes so frequently observed in the parameters (trend shift) cannot be explained within the framework of any of these models. This casts doubt on the whole approach, and makes unconvincing the assertion concerning the "special" stability of such a highly aggregated indicator as monetary velocity.

Since the proportions between monetary velocity, growth of output, and increase in prices do not, as a rule, fit into the elementary monetarist scheme, its advocates broadly assume the existence of lags in the development of the inflationary process. The duration of these lags, however, continues to be a controversial issue. It follows from Friedman's reasoning, for instance, that these lags may come to between three and seven quarters, depending on the initial conditions, changes in the structure of the economic mechanism, etc. Friedman believes, in particular, that with

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[1] Let us consider, for instance, the elementary Keynesian model of income formation (for there are simply no such monetarist models). Let the role of independent variables in the model be the influx into the economic system of an additional quantity of money as a result of "autonomous" investment. But in that case it follows from the monetarist assumption concerning the stability of monetary velocity that there is a clear and stable connection between "autonomous" investment and the aggregate income (from the operation of the acceleration mechanism), i.e. the conclusion concerning the stability of the key correlation of the Keynesian scheme, the marginal propensity to consume.

the growth of money supply becoming ever more irregular, these lags should become shorter. Some other economists say that in the postwar period these lags have been very much shorter.[1] Since monetarists do not have in their possession advance information about the length of these lags, the structure of the model turns out to be insufficiently definite. So, if the movement of production and prices cannot be explained by changes in money supply (say, over the preceding six months or a year), "the day can be saved" by a simple reference to the changing length of the lags.

The monetarists say that the instability of money supply is the main cause of inflationary price growth and instability of economic development generally. But in practice it is quite possible to have situations where major upheavals in the economic system break out when the growth of money supply is more or less stable. Thus, the cyclical growth and subsequent decline in production in the United States from 1971 to 1974, the rapid acceleration of the inflationary growth of prices in that period, the sharp disruption of equilibrium in the balance of payments and monetary relations, etc. were attended, as Modigliani and Papademus showed, by the most stable rate in the increase of money supply over the postwar period.[2]

According to the monetarists, the influence of prices on factors outside the sphere of money circulation should be fullest over the long term, and even on the strength of the quantity theory assumptions, the increase in money supply should lead to an increase in the money value of the realised

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[1] A. A. Walters, a leading British monetarist, says that an average of roughly two quarters elapse between implementation of regulating measures in monetary policy and price changes. (A. A. Walters, *Money in Boom and Slump*, Published by the Institute of Economic Affairs, London, 1969, Hobart Paper 45, p. 38.)

[2] The growth of money supply over this period fluctuated round 7 per cent by no more than one percentage point.

product. The proportion in which this increment will be distributed over a period of several years between the growth of physical output and prices depends on a number of concrete economic conditions, like the phase of the cycle, the existence of underloaded capacities, etc.

Some aspects of the interaction between money supply and the supply of commodities on the market have been elaborated in greater detail in the Keynesian concept of inflation.

2. The Keynesian Concept

The emergence of the Keynesian concept of inflation is frequently linked with the publication in 1936 of Keynes's *The General Theory of Employment, Interest and Money*, but we find that Keynes was not sufficiently consistent in his statements concerning the theory of prices and the theory of money.[1] This is due to a number of reasons, the most important being the marked evolution of his view of inflation.

Keynes was among the Western economists who began to regard inflation immediately after the First World War, not as some kind of sporadic anomaly in the development of money supply, but as one of the most probable trends in the subsequent development of the capitalist economy.

He wrote: "This progressive deterioration in the value of money through history is not an accident."[2]

Keynes was seriously alarmed over the prospect of the continued depreciation of money, for he

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[1] Samuelson once ironically remarked that "if Parliament were to ask six economists for an opinion, seven answers would come back—two, no doubt, from the volatile Mr. Keynes" (Paul A. Samuelson, "What Economists Know". In: *The Human Meaning of Social Sciences*, Ed. by D. Lerner, Meridian Books, Inc., New York, 1959, p. 192).

[2] John Maynard Keynes, *A Tract on Monetary Reform*, Macmillan & Co., London, 1923, p. 9.

saw it as a threat to the very existence of the capitalist system. He wrote:

> "There is no subtler, no surer means of overturning the existing basis of society than to debauch the currency."[1]

As the inflationary process escapes control, he said, it tends to cause initially imperceptible processes which inexorably erode the foundations of capitalist relations.

Keynes was not alone in being alarmed over the consequences of rapid development. Another prominent British bourgeois theorist, R. G. Hawtrey, wrote:

> "Inflation is a deadly blight; once it has gained a hold, it will poison the whole economic system, and can only be eliminated, if at all, at the cost of exhausting efforts."[2]

Keynes believed that the main cause of inflation lay in the fact that the Treasury was always short of money, so that the government most frequently tried to cover the deficit by resorting to a covert inflationary tax. That is why in the 1920s, Keynes, like many others who took the orthodox view of financial theory, opposed "excessive" increases in government spending.

In *A Treatise on Money*, which was published in 1930, Keynes proposed a more general concept of inflation as stemming from the relation between prices in cash transactions and prices in futures. He believed that an increase in the former as compared with the latter was a sign of "commodity inflation", and in the latter as compared with the former, of "income inflation" because an increase in market supply always entailed, according to

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[1] John Maynard Keynes, *The Economic Consequences of the Peace*, Macmillan & Co., London, 1920, p. 220.

[2] R. G. Hawtrey, *Currency and Credit*, Longmans, Green and Co. Ltd., New York, 1928, p. 250.

Keynes, a growth of money payments to the owners of production factors.[1]

The economic crisis of 1929-1933 and the protracted depression that followed demonstrated the impotence of bourgeois economic theory, which operated with static microeconomic schemes of equilibrium and, in effect, ruled out the possibility of any serious economic upheavals. One economist wrote: "There was no longer equilibrium in fact, and there could no longer be equilibrium in theory."[2] All of this induced Keynes to take a fresh look at the problem of inflation. In *The General Theory of Employment, Interest and Money*, he concentrated on the inadequacy of effective demand, but because inflation, according to his light, was connected with the opposite situation—an excess of effective demand—he said relatively little about the problem in that book.[3] But what is important is not only Keynes's emphasis on situations characterised by limited effective demand. In his new work he gave a different description of the market mechanism itself, his reasoning now being centred on the idea that the immediate result of an increase in money demand in normal conditions is a growth in physical output and employment, while prices are set in motion only in the presence of some additional conditions.[4]

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[1] John Maynard Keynes, *A Treatise on Money*, Vol. II, Macmillan & Co., London, 1930, pp. 155-157.

[2] G.L.S. Shackle, *The Years of High Theory. Invention and Tradition in Economic Thought. 1926-1939*, Cambridge University Press, Cambridge, 1967, p. 290.

[3] Accordingly, some economists believe that there is no Keynesian concept of inflation at all (see, for instance, *Inflation Theory and Anti-Inflation Policy. Proceedings of a Conference held by the International Economic Association*, Ed. by E. Lundberg, Macmillan & Co., London, 1977, p. 130.

[4] The usual Keynesian "input-output" scheme generally turns to limit the sphere of analysis to a fairly narrow range of "real magnitudes". Hicks ironically mentions some "neo-Keynesians" who think only in categories of employment and output, and are prepared to ignore prices altogether.

In such schemes, the inflationary growth of prices in most cases has to be preceded by favourable changes in the real sector of the economy: an expansion of output and a drop in unemployment. From here it was only one step towards the conclusion, always implied but never explicitly formulated, concerning the stimulating effect of inflation on the course of economic development. This necessarily had an influence on the earlier views of inflation, especially when it came to an inflationary increase in money demand that was maintained within definite limits (as expressed, for instance, in "creeping inflation"). One cannot assert, of course, that this converted all the economists into active proponents of inflation, but since the 1929-33 crisis, a stable system of values has taken shape in Western theory according to which "moderate" inflation is not as acute a socio-economic problem as, say, massive unemployment, and does not require primary attention from theorists, so naturally slowing down further research. In the mid-1970s, one of the best-known students of Keynesian theory, Leijonhufvud, had good reason to assert the following:

> "But the economics profession as a whole has not done its homework on inflation... Theoretical analysis and empirical research alike have been neglected—presumably *because* of the attitude that inflation is not such a serious problem. The new view just is *not* on solid ground."[1]

At the same time, in his *General Theory* Keynes changes the very framework of economic analysis. The operations by individual economic agents, who used to be central to the analysis in *A Treatise*

(J. Hicks, *Economic Perspectives. Further Essays on Money and Growth*, Oxford, 1977, p. XIII.)

[1] A. Leijonhufvud, "Costs and Consequences of Inflation". In: *The Microeconomic Foundations of Macroeconomics*, Ed. by G. Harcourt, Macmillan, London, 1978, p. 301.

on Money, were now no longer of great consequence,[1] for Keynes now considered mainly the interaction of aggregate magnitudes, which is why his definition of inflation was different. "True" or "absolute" inflation, according to Keynes, occurred

> "when a further increase in the quantity of effective demand produces no further increase in output and entirely spends itself on an increase in the cost-unit fully proportionate to the increase in effective demand."[2]

A US economist who supports this view, has given a more concise definition of inflation: "an excess of demand over supply".[3]

However, prices can start to grow even before the "full employment" of all the production factors is reached. That is why Keynes introduced the concept of "semi-inflation", which appears on the scene after the economy has passed the "semi-critical" points, where "a further increase in effective demand in terms of money is liable to cause a discontinuous rise in the wage-unit".[4]

Very little attention is given to the mechanism of inflation. So long as private economic operations are examined, the only factor which within the framework of the Keynesian scheme can influence the scale of money supply is the market rate of interest, which is why "true inflation" may result from a drop in interest rate below the level which corresponds to "full employment".[5] In one interpretation of Keynesian theory, for instance, inflationary growth of prices is derived from an ex-

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[1] A. Hansen, *A Guide to Keynes*, McGraw-Hill Book Company, New York, 1953, p. 44.

[2] John Maynard Keynes, *The General Theory...*, p. 303.

[3] Abba P. Lerner, "The Inflationary Process". In: *The Review of Economics and Statistics*, Vol. XXXI, August 1949, No. 3, p. 194.

[4] John Maynard Keynes, *The General Theory...*, pp. 301-302.

[5] *Ibid.*, pp. 202-203.

cess of actual investment over savings caused by the drop of interest rate below the equilibrium level.[1]

The experience of the 1930s gave a visual demonstration of the limitations of the elementary monetarist concept.[2] From the outset, Keynes regarded the additional issue of money as a factor increasing income ("the new money becomes someone's income"). A part of the additional income is kept in the form of cash. There are two types of money demand:

1) demand for cash required for commodity transactions and kept "just in case", M_1; and

2) accumulation of monetary reserves used for operations involving financial assets, M_2 ("speculative demand for money").

Keynes examined in detail the possible influence of the market interest rate on M_1 and M_2, an approach which allowed him to take into account possible changes in monetary velocity and to link them with fluctuations in interest rates.

Another necessary element of the Keynesian concept of inflation is the idea of the limited potentialities for further expansion of production facilities. In one of his last works, Keynes defines inflation:

> "By *inflation*... we should mean the increase of purchasing power corresponding to which there is no accompanying increase in the quantity of production."[3]

The growth of money supply in an economic system that has not yet attained a state of "full employment" may stimulate the growth of produc-

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[1] See: Lawrence R. Klein, *The Keynesian Revolution*, the Macmillan & Co., New York, 1947.

[2] "The definition of inflation as an increase in the amount of money ... was not able to survive the 1930s" (Abba P. Lerner, "The Inflationary Process", p. 193.)

[3] *The New Economics. Keynes' Influence on Theory and Public Policy*, Ed. by Seymour E. Harris, New York, Alfred A. Knopf, 1948, p. 397.

tion.[1] However, at a certain point continued growth of the propensity to consume comes up against the short supply of this or that production resource (many advocates of this view of inflation are inclined to see the shortage of labour power as the chief obstacle to expanding production)[2] and the inadequacy of commodity stocks. This gives a push to the "semi-inflationary" growth of prices, including prices for some production factors.[3] As the potentialities for further expanding production and approaching the full employment of all resources are worked out, the inflationary process gathers momentum, and the "inflationary gap" between effective demand and commodity supply which this produces can be overcome only through a further growth of prices.

With the publication of Keynes's *The General Theory of Employment, Interest and Money*, thy new macroeconomic concept of inflation, widely accepted among Western economists, increasingle lost touch with the microeconomic analysis of price formation.[4] The "inflationary gap" idea was always an essential element of these schemes. Thus, Bent Hansen's scheme considered in detail the in-

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[1] In the light of the experience of the 1930s, Keynes was very cautious in his formulations:

> "If, however, we are tempted to assert that money is the drink which stimulated the system to activity, we must remind ourselves that there may be several slips between the cup and the lip." (John Maynard Keynes, *op. cit.*, p. 173.)

[2] See: N. Kaldor, "Economic Growth and the Problem of Inflation". In: *Economica*, Vol. XXVI, August 1959, No. 103, p. 216.

[3] The idea of semi-inflationary price growth is considered in greater detail by A. Hansen, "Cost Functions and Full Employment". In: *The American Economic Review*, Vol. XXXVII, September 1947, No. 4, pp. 552-565.

[4] Describing the wholesale enthusiasm over aggregated schemes and models, Eric Roll ironically termed it a "disease of 'macro-economicosis'." (Eric Roll, *The World After Keynes. An Examination of the Economic Order*, Pall Mall Press, London, 1968, p. 69.)

teraction of the processes generated by the "inflationary gap". The motive forces of inflation are ultimately reduced to an excess of money demand over supply under the given (initial) prices. Hansen assumes that neither the monetarist, nor the Keynesian concepts are capable of explaining the change in the purchasing power of money, without using the idea of an excess of demand over supply.[1]

The assumption concerning the constant scale of production made the whole Keynesian concept of inflation highly static. In the subsequent period, some economists tried to get rid of this premise, and parameters characterising elasticity of commodity supply were included in some models of economic growth. The possibility of expanding production over a long term is determined above all by the real accumulation: growth rates under which investment is equal to real savings were designated by Harrod as "guaranteed". Since there can be no further expansion of production by definition, the impact of the initial impulse may prove to have been worked out only because the propensity to save tends to increase with the growth of nominal income. But such an assumption may clash with the whole history of inflation: accelerating price growth inflicts considerable losses on the owners of monetary liabilities, which is why at a definite stage of the process the incentives to keep savings in money form are reduced.

Arguing against the "primitive" treatment of price formation within the framework of the equation of exchange (the Fisher equation), the Keynesians questioned the use of the category of monetary velocity itself. In his *General Theory*, Keynes wrote that the term "income-velocity of money" (V) could be misleading, because there is a demand only for a part of the money proportional to in-

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[1] Bent Hansen, *A Study in the Theory of Inflation*, pp. 250-251.

come. Besides, "there is ... no reason for supposing that V is constant".[1] Alvin Hansen, one of Keynes's best-known followers, wrote: "I think we should do well to eliminate, once and for all, the phrase 'velocity of circulation' from our vocabulary," because the actual role of this parameter remains unclarified,[2] while another US economist declared that "velocity of money is a discredited subject".[3]

The Keynesian concept of inflation implies a somewhat more general approach to the problem of inflation (as compared with the elementary monetarist concept). It turns out that the Keynesian schemes make it possible to take into account the influence of some factors lying on the side of production, like the movement of production capacities. But both with the monetarist and the Keynesian approach, inflation is frequently reduced to an "excessive" growth in money supply. As soon as the influence of the additionally issued money meets with the impossibility of further expanding production, the description of the inflationary process by the Keynesians and the monetarists is almost completely identical. The subsequent development of the process, according to Keynes, fully corresponds to the quantity theory of money, "for output does not alter and prices rise in exact proportion to MV".[4]

Keynesian models allow the separate examination of the movement of money supply and changes in effective demand by tying in monetary velocity with the movement of the market interest rate. But even here, the difference between the Keynesian

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[1] John Maynard Keynes, *op. cit.*, pp. 194, 201.

[2] Alvin H. Hansen, *The American Economy*, McGraw-Hill Book Company, New York, 1957, p. 50.

[3] Ernest M. Doblin, "The Ratio of Income to Money Supply: An International Survey". In: *The Review of Economics and Statistics*, Vol. XXXIII, August 1951, No. 3, p. 201.

[4] John Maynard Keynes, *op. cit.*, p. 289.

and the monetarist approach is not substantial, and one monetarist, R. Selden, says:

> "Once the dust settled after the 'Keynesian Revolution', it became increasingly apparent that there was no conflict between this way of looking at money and the traditional velocity approach."[1]

The differences between the neoclassical and Keynesian lines on this issue are perhaps most pronounced in the description of the mechanism of short-term response by the economy to an increase in money supply. Excessive money supply, the monetarists think, should increase spending, so directly stimulating prices and money incomes. The Keynesians believe that a change in the money supply has an effect above all on the ratio between liquidity demand and supply, so causing a change in interest rate. A rise or fall in interest rate has an effect on investment, and this, for its part, sets in motion the multiplicator mechanism, so producing a corresponding increase (or decrease) in personal income. The index of prices (of some prices at any rate) remains fixed so long as the growth of investments does not meet with the shortage of some production resources; consequently, the growth of money supply in conditions of "underemployment" stimulates the economy, leading primarily to a growth of income, and not to a general rise in prices.

In this context, there is a difference in the definition of short- and long-term periods. The monetarists usually regard a long-term period as an interval of time over which all the "expectations" are realised (expected prices, expected output, and consequently, expected profits).[2] The Keynesians

[1] *Studies in the Quantity Theory of Money*, Ed. by Milton Friedman, the University of Chicago Press, Chicago, 1956, p. 233.

[2] Thus, Friedman remarked that such a long-term period may mean "a couple of decades" (M. Friedman, "The Role of Monetary Policy". In: *The American Economic Review*, March 1968, p. 11).

see a long-term period as one in which fresh production investments can be commissioned, and a short-term period, as one in which firms operate within the limits of old production capacities.[1]

In the Keynesian view of the mechanism of inflation, the role of the rate of interest is hypertrophied.[2] Such theoretical notions clash not only with the whole record of the development of capitalist economic relations, but even with Keynes's own cautious remarks upon the failure of monetary and credit policy in the 1930s.[3]

There is also a serious inner contradiction in the Keynesian notions of the results of expanded effective demand. After all, seeking to make their theoretical reasoning more realistic, Keynes and his followers admitted that under modern capitalism the potentialities of competition were limited (in some sectors of the economy, at any rate), and the market mechanism insufficiently flexible. But they completely ignored the fact that this produced other forms in which economic relations were realised, above all, the role of regulation of market supply and the development of the trend towards a one-sided mobility of prices. Meanwhile, the erosion of the old system of free competition produced new situations in which an expansion of the market in

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[1] Let us note the following essential point: for the non-monetarists, "it is the long run which is irrelevant because it is far away, and the short-run response is the only one that matters", says Franco Modigliani. (*The American Economic Review*, May 1975, No. 2, p. 181.)

[2] Robertson ironically remarked that "nothing was ever allowed to happen—money was not allowed to affect prices, wage-rates were not allowed to affect employment, I had almost added, the moon was not allowed to affect the tides—except through the rate of interest". (D. Robertson, *Essays in Money and Interest*, Collins, London, p. 188.)

[3] Keynes said: "It seems likely that the fluctuations in the market estimation of the marginal efficiency of different types of capital ... will be too great to offset by any practicable changes in the rate of interest." (*General Theory...*, p. 164.)

the presence of underloaded production facilities could lead not only (and in some cases, even not so much) to an increase in total output and employment, as to a steady growth of prices. This has become perfectly obvious over the past few years.[1]

One will still find in Keynes's *General Theory* some mention of the real factors shaping the system of relative prices, and of the influence which that system has on changes in economic activity and level of employment. But the impact of inflation on the price structure has, in effect, disappeared from the sphere of theoretical analysis. In the works of Keynes's followers, the analysis of price movements is most frequently confined to the influence of aggregate effective demand on the movement of the general price level, and here the assumptions concerning the sensitivity of absolute prices to changes in effective demand are fairly artificial. Thus, up until the attainment of a definite level in the employment of resources, changes in demand have no effect on prices; but when that point has been reached, the movement of prices depends only on market demand.

This contrast is not very convincing, and this is why the division of the economic process into a state of underemployment and "absolute inflation" appears to be tentative as well. Suffice it to say, for instance, that the most rapid inflationary growth of prices, which occurred in a number of industrialised capitalist countries in the postwar period, was not connected with any marginal intensive use of material and labour resources, even if one takes into account the potentialities available under the domination of the capitalist relations of production.

[1] "Keynesian remedies to monopolistic lapses from full employment may henceforth require not merely inflation, but an accelerating inflation. This compels us to look for other 'means to prosperity'," declares Herbert Giersch, Director of the Kiel Institute of World Economics. (H. Giersch, "Some Neglected Aspects of Inflation in the World Economy". In: *Public Finance*, Vol. XXVIII, No. 2, 1973, p. 108.)

What is more, "galloping inflation", for its part, produces a trend towards growing disproportionality and a chaotic movement in the individual industries and spheres of the economy. At a definite stage in the development of the inflationary process, this trend tends to disrupt the intricate economic mechanism, owing to which the rapid inflationary growth of prices is, as a rule, combined with a decline in the share of manpower and material resources engaged in production. Thus, despite the intense development of "demand inflation" in Germany after the First World War, there was greater underloading of capacities in the country, and unemployment (especially partial) was greater than, say, during intense cyclical upswings.[1]

There was an even more striking contradiction between Keynesian forecasts and the actual movement of the general price level in time of economic crisis. The development of the capitalist economy since the Second World War has shown that the general price level can go up even with an overaccumulation of capital and sizable unemployment, a fact which has brought out most vividly the limitations of the Keynesian macroeconomic approach, which deals only with aggregate money demand and the general characteristics of the use of production resources. That is why the theory of so-called new inflation, or "cost-push" inflation was put forward as an alternative to it.

3. The "Cost-Push" Inflation Concept

The neoclassical concept of inflation examines no more than the movement of prices under the influence of competitive forces. The neoclassics do,

[1] In *A Tract on Monetary Reform* Keynes was compelled to state that the rapid development of inflation in Germany in the early 1920s had virtually paralysed the whole of the economic life.

of course, mention only oligopolistic or monopolistic price formation, but they invariably go on to assert that such relations alone cannot be regarded as being typical of present-day capitalism. Hence their denial of any role of monopoly price regulation in the development of contemporary inflation.[1]

The theoretical constructs according to which the development of inflation does not depend on the acts of oligopolistic firms is directly used by Big Business in the course of all kinds of investigations, congressional hearings, and so on. Thus, Roger M. Blough, Chairman of the Board of the United States Steel Corporation, used the following line of argument at one congressional hearing: "Rising prices do not cause inflation; they are the result of inflation."[2] From this, he suggested, there followed this conclusion (as simple as it was convenient for Big Business): giant corporations have no active role to play in the inflationary process and, finding themselves to be "victims" of inflation, are simply "forced" to adapt themselves to it by raising prices.

But the actual picture of economic development turns out to be in crying contradiction with such notions. Thus, in conventional neoclassical models, economic agents should have responded to a reduction in market demand by lowering prices. But even the relatively deep cyclical crisis of 1957-58 did not fully stop the upward movement of prices; in the subsequent period, the trend towards a growth of prices during economic

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1 In this context, let us recall Stigler's ironic suggestion that "economists might serve a more useful purpose if they fought fires or termites instead of monopoly". (George J. Stigler, "The Statistics of Monopoly and Merger". In: *The Journal of Political Economy*, Vol. LXIV, February 1956, No. 1, p. 34.)

2 *Administered Prices. Hearings before the Subcommittee on Antitrust and Monopoly Committee on the Judiciary United States Senate. 85 Congress, 1st Session*, Government Printing Office, Washington, 1958, p. 204.

stagnation and recession continued to advance, producing such new concepts as "stagflation" and "slumpflation". The 1974-75 crisis and the subsequent flabby revival of business activity were attended by a continued (and in some instances, even accelerated) rise in prices, so demonstrating the irrelevance of the elementary schemes which linked the inflationary process only with the free play of competitive market forces.[1]

The specifics of capitalism's contemporary economic development have induced bourgeois economists broadly to accept a new concept of inflation. Since the second half of the 1950s, there has been a steady flow of books and articles on the "new inflation", on "cost-push", "administered prices", "sellers' inflation", "income inflation", etc. Some of those who had earlier taken the Keynesian view, were now forced to admit that the general increase in prices with the growing underloading of production capacity testifies to the development of a new type of inflation, namely, "cost-push inflation".[2]

As a result, inflationary situations were classified under two heads: "demand-pull" and "cost-push" inflation. Some even tried to apply the same classification to the various periods of economic development: thus, one economist said that from 1946

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[1] "Today's world hardly appears consistent with the classical equilibrium interpretation of output fluctuations based on errors in forecasting prices. A large worldwide gap between actual and natural output has persisted in 1976-78 in the face of a relatively steady and well-predicted inflation rate" (Robert J. Gordon, "What Can Stabilisation Policy Achieve?" In: *The American Economic Review*, May 1978, Vol. 68, No. 2, p. 338.)

[2] See, for instance, the statement by A. Lerner ("The Relationship of Prices to Economic Stability and Growth", *Compendium of Papers Submitted by Panelists Appearing before the Joint Economic Committee, US Congress*, Washington, March 31, 1958, pp. 257-273.)

to 1948 the United States had "demand' and from 1955 to 1957, "cost" inflation.[1]

The Keynesian concept gave little attention to the microeconomic interplay of costs and prices on the level of an individual firm, emphasising the assumption about the relatively lesser mobility of the "unit wage" (that is, money wage per unit of labour).[2] By contrast, the "new inflation" theorists emphasise the influence that changes in costs have on the whole price-formation process.

The cost inflation concept has always been somewhat contradictory. On the one hand, it connected the possibility of a rise in the general price level with the limitation of the sphere of free competition and the growing role of non-competitive factors in economic development. On the other hand, traditional microeconomic theory has always inclined to the idea that transition to oligopoly or monopoly can result only in a one-shot increase in prices, and that in the subsequent period it tends to give the existing price system greater stability. Thus, in Haberler's view, the transition to monopoly in business activity could cause a short-term rise in prices but could not be a source of any protracted growth in the consumer price index.[3] Elaborating the theoretical definition of

[1] Edmund S. Phelps, "A Test for the Presence of Cost Inflation in the United States 1955-57". In: *Yale Economic Essays*, Vol. 1, No. 1, Spring 1961, pp. 28-69.

[2] Sixteen years after the *General Theory* was published Haberler wrote: "It is now almost generally recognised that the Keynesian theoretical system proper ... depends on the assumption of wage rigidity. If that assumption is not made, the Keynesian system simply breaks down or, to put it differently, it loses its distinctive and differentiating quality which sets it apart from what is loosely called the 'classical' system". (Gottfried Haberler, "Sixteen Years Later". In: *Keynes' General Theory. Reports of Three Decades*, Ed. by Robert Lekachman, St. Martin's Press, New York, 1964, p. 291.)

[3] Gottfried Haberler, "Internal Factors Causing and Propagating Inflation: I". In: *Inflation, Proceedings of a Conference Held by I.E.A.*, London, 1962.

cost inflation, Phelps from the outset rules out any situations connected with a strengthening of the monopoly positions of businessmen or trade unions, because in such cases there is only a short-term rise in prices.[1]

According to traditional macroeconomic theory, prices must be especially stable in the oligopoly sector, and the demand-curve is being increasingly used to back up this idea.[2]

The essence of this line of argument boils down to the following. Under monopoly competition, an individual firm as a rule, avoids reducing prices, for in that case it will be unable to compensate its losses through a sharp expansion of its share in aggregate sales, because its rivals will follow it by reducing their own prices. On the other hand, an oligopoly firm, is unwilling to raise prices, because its rivals will not follow suit, since their prices will be lower, and the firm with the higher prices will be unable to find any buyers. The suggestion here is that for each of the partners involved in oligopolistic relations it is preferable to maintain the old price.

This view, assuming a "break" in the demand-curve at the point characterising the market price which has taken shape at the given moment is usually used to describe oligopolistic price formation. In the recent period, however, Phelps and Winter[3] have proposed a more general microeconomic scheme in which certain stability of prices is ensured by the urge on the part of buyer firms

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[1] Edmund S. Phelps, *op. cit.*, p. 36.

[2] The demand-curve theory was first elaborated in P. Sweezy's "Demand under Conditions of Oligopoly". (In: *The Journal of Political Economy*, Vol. XLVII, August 1939, No. 4, pp. 568-573). In the subsequent period, it became a part of all texts on microeconomic theory and industrial organisation.

[3] See: *Microeconomic Foundations of Employment and Inflation Theory*, by Edmund S. Phelps et al., W. W. Norton & Co., Inc., New York, 1970.

to minimise the costs incidental to the search for more advantageous terms of purchase. Accordingly, buyers will reduce their demand for the product of firms whose prices are subject to the greater fluctuations, and increase their purchases from firms responding to changes in market demand by switching to new output and by maintaining stable prices. While this line of argument, generally speaking, can apply to any economic agents, it is only the large firms that are clearly able to manoeuvre in the sphere of market supply and to maintain more or less stable prices.

On the strength of the broken demand-curve and other similar theoretical constructs, many economists regard the functioning of the oligopoly sector not as one of the chief sources of inflation, but rather as a barrier to inflation and the bulwark of price stability. Weston says that the large firms are a strong barrier in the way of rising prices: "The overall pressures for price increases have been blunted in the most concentrated industries."[1] Jacoby also believes that because of the monopoly power of big companies, the effect of their prices on the consumer price index has been less inflationary.[2]

E. Mason, who has written a number of works on the theory of monopoly and oligopoly firms, says that the oligopoly sector of the economy usually takes every opportunity to maintain the old prices when expanding production, and is forced to review these only in extreme cases. It is always the small and middle firms, he claims, that raise prices, which is why "public authorities should thank heaven for a substantial degree of

[1] J. Fred Weston, "Large Firms and Economic Performance". In: *The Impact of Large Firms on the U. S. Economy*, Ed. by J. Fred Weston, Stanley I. Ornstein, Lexington Books, Massachusetts, 1973, p. 228.

[2] Neil H. Jacoby, "Myth of the Corporate Economy". In: *Large Corporations in a Changing Society*, New York University Press, New York, 1975, pp. 137-138.

concentration in the American economy".[1] This idea has migrated into the theoretical schemes describing the so-called new industrial society. Indeed, Galbraith, in effect, reproduces the ideas behind the broken demand-curve: the prices set by firms have a tendency to be unchanged for long periods, "since any substantial movement invites the risk that others will not follow".[2]

Many Western economists are inclined to regard the functioning of trade unions and organised action by the working class for higher wages as a monopoly position on the labour market. In contrast to manufacturers' unions, such a monopoly, the advocates of "cost inflation" claim, is usually an important factor behind the growth in the price index. That is why bourgeois economists most frequently assert that wages are the key element of the costs which sets in motion the whole "cost-price" system. Here is what some of them said in the late 1950s and early 1960s. The US economist Arthur Smithies wrote: "In the United States, inflation is intimately bound up with the wage-price spiral."[3] One collective work claimed that aggressive pricing to raise profit margins was not the starting cause of inflation, whereas an increase in wages instantly sets in motion the wage-price spiral.[4] The most characteristic claim about the role of trade unions in pushing up inflation was made by Chamberlin, who asserted that trade unions were the key source of monopolisation of the whole of economic activity, and that they

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[1] Edward S. Mason, *Economic Concentration and the Monopoly Problem*, Atheneum, New York, 1964, p. 171; J. Downie, *The Competitive Process*, Duckworth, London, 1958, pp. 109-110.

[2] John Kenneth Galbraith, *The New Industrial State*, Houghton Mifflin Co., Boston, 1967, p. 180.

[3] Arthur Smithies, "The Control of Inflation". In: *The Review of Economics and Statistics*, Vol. XXXIX, August 1957, No. 3, p. 272.

[4] *The Problem of Rising Prices*, OEEC, 1961, p. 70.

were entirely to blame for the development of contemporary inflation.[1]

Other economists, like J. Clark, assume that

> "a progressive increase in wage costs, at the rates we have been recently experiencing, if absorbed out of profit margins—already a minority share—would in less than a decade reduce these margins below the minimum necessary to the function they perform in our kind of economy."[2]

These predictions were made nearly twenty years ago, and since that time capital has been accumulated at an accelerating pace. Still, despite the clear failure of such predictions, their number has continued to grow, and perhaps never before have so many apprehensions been expressed over the rise in nominal wages and fall in the rate of profit as in the 1970s.[3] This turns the growth of wages into a "scapegoat", according to Cagan. The struggle carried on by factory and office workers to improve their living standards (and under accelerating inflation, also to maintain their old standard) is declared to be the main cause of economic stagnation and inflationary price growth.

Let us note that those who take this approach do not connect the movement of wages with objective economic processes. What is more, because there is no common general theory of "wage inflation" (and some claim that there can never be

[1] Edward H. Chamberlin, *The Economic Analysis of Labor Union Power*, American Enterprise Institute for Public Policy Research, Washington, 1963.

[2] John Maurice Clark, *Competition as a Dynamic Process*, The Brookings Institution, Washington, 1961, p. 451.

[3] To give one example from 1977: if current economic events are destined to result in the collapse of capitalism, it is because the growth of wages has so reduced the profitability of capitalist enterprise that it can no longer survive. (D. C. Hague, "A Summing Up". In: *Inflation Theory and Anti-Inflation Policy*, Ed. by Erik Lundberg, The Macmillan Press Ltd., London, 1977, p. 533.)

one), there have been suggestions that the problem lies outside the framework of political economy. In such cases, the analysis of the sources of wage inflation is simply confined to references to "excessive claims" by the working class and the "excessive" power of the trade unions.[1] Nor is there any theoretical back-up for an economic mechanism that would ensure a growth of prices in accordance with the growth of costs. In order to bridge the "wage inflation" concept and monetarist theory there is ever greater resort to the idea that the central bank's monetary and credit policy fully or partially depends on the activity of trade unions. Summing up the results of an International Economic Association conference on inflation, Hague said that

> "trade unions seemed recently to have been quite successful in ensuring that the money supply was increased to ensure that higher wages could be paid".[2]

Others say that the question of money supply does not generally have any essential role to play because money policy has been "adjusted" to the requirements of full employment, and almost automatically ensures an increase in money supply with the growth of wages. The neglect of the role of the monetary and credit mechanism in the development of inflation which is typical of the advocates of the "wage-price" spiral concept is just as one-sided as the absolutisation of this mechanism by the monetarists.

The concept of cost inflation certainly reflects

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[1] Hicks says that in practice explanations of cost inflation usually boil down to ascribing inflation to the aggressiveness of trade unions, but according to this logic, one would have to say that the growth in the rate of inflation results from the growing "aggressiveness" of the labour unions. (J. Hicks, *Economic Perspectives. Further Essays on Money and Growth*, Oxford, 1977, p. 108.)

[2] D. Hague, "A Summing-Up", p. 530.

the real growth of social conflicts in the capitalist society today, but it does so in irrational and biased forms, declaring in advance that the demands made by a majority of the population are the only source of inflation, and regarding inflation as the best way of resolving the sharpening contradictions between the social classes. Thus, James Tobin said in his presidential address to the American economic association that the alternative to inflation could be "worse" methods of resolving social conflicts, whereas

> "inflation lets this struggle proceed and blindly, impartially, impersonally, and non-politically scales down all its outcomes".[1]

The distinction between demand inflation and cost inflation, so often refuted and again revived in Western economic writings, has been fairly artificial from the outset. It can be easily demonstrated, for instance, that among the conditions making cost inflation possible is a corresponding increase of money demand. On the other hand, the cumulative growth of prices under demand inflation has always implied an interaction between costs and prices (price growth leads to a growth of costs, which under certain economic conditions can lead to a further growth of prices, etc). That is why the mechanism of any inflationary process running over a sufficiently long period inevitably involves both economic links characterising demand inflation and links characterising cost inflation. The two components closely interact with each other, and in most instances it is virtually impossible to isolate them.[2]

[1] James Tobin, "Inflation and Unemployment". In: *The American Economic Review*, March 1972, Vol. LXII, No. 1, p. 13.

[2] A similar situation can be observed on the microeconomic level as well. Arrow pointed to the inadequacy of the traditional microeconomic constructs for analysing price movements and said, in particular, that in a sense

Seeking to deny the role of monopoly enterprise in pushing up the consumer price index, orthodox economic theory now usually tries to bring out artificial economic situations in which there is either a free play of market forces or "pure monopoly" (with the latter most frequently seen simply as a situation temporarily taking shape on some markets). Fresh theoretical schemes fail to take account of the fact that oligopoly may increase the sphere of its influence and economic strength, while having to face market forces beyond oligopoly regulation. But the fact is that under present-day capitalism it is the interaction of two opposite elements—monopoly and competition—that is invariably the actual source of price movements. Lenin saw the most essential feature of monopoly capitalism in a contradictory combination of monopolies with exchange, market, competition, and crises.[1]

The contradictory unity of monopoly and competition cannot rule out the spontaneous operation of market factors, which, first, generates new economic mechanisms of price increases in which the active impulse may come from the oligopoly sector, and second, modifies the "passive" response of prices to the impulses coming from changes in market demand. As a result, the processes leading to a cut in the prices of the products of the big corporations meet with a number of constraints, while the higher cost of commodities proves to be ever more stable.

At the same time, the trend towards a long-

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inflationary processes could be referred to cost inflation "in that it is the monopoly power resulting from excess demand which is their proximate cause... Those who see cost inflation may be looking at an immediate causal factor, while those who speak of demand inflation have their eye on a more ultimate stimulus". (Kenneth J. Arrow, "Toward a Theory of Price Adjustment". In: *The Allocation of Economic Resources*, Stanford University Press, Stanford, 1959, p. 50.)

[1] V. I. Lenin, *Collected Works*, Vol. 24, Progress Publishers, Moscow, 1964, p. 464.

term and irreversible growth of prices, inherent in oligopoly price formation, can be expressed only in dynamic situations, a fact which is completely ignored in static microeconomic constructs. Marx noted that in practical life we find not only monopolies, competition and their antagonism, but also their synthesis, and emphasised that this synthesis is not a formula but a movement.[1] Thus, the primary factor setting prices in motion may prove to be cyclical changes in economic activity, the structural remodelling of the economy, etc. But as these primary impulses are manifested and realised, they may be modified by oligopoly and government regulation of market supply and demand.

Schemes based on the "kinky demand-curve" also prove to be untenable. Let us note, first of all, that such schemes say nothing about why prices have reached this or that level. Because the reasoning about the "kinky demand-curve" only suggests the stability of "oligopoly prices", let us confine ourselves to examining to what extent competition within group monopoly may be a special obstacle to price growth.

The "kinky demand-curve" scheme assumes that relations between a few giant firms may ultimately be reduced to the common forms of price rivalry which is characteristic of free competition. But in present-day conditions, these relations are not only competitive but also monopolistic: thus, the big firms fairly soon concert their activity even when they fail to conclude formal agreements with each other. One widely adopted system is that of price leadership, under which the leading firm raises its prices on the assumption that all the other companies will always follow suit (whereas the "kinky demand-curve" assumes that its com-

[1] Karl Marx, "The Poverty of Philosophy". In: Karl Marx, Frederick Engels, *Collected Works*, Vol. 6, Progress Publishers, Moscow, 1976, p. 195.

petitors will not raise their prices). The data concerning the movement of prices fixed by the biggest companies in steel, automobile, pharmaceutical, and certain other industries in the United States testify to the exceptionally efficient coordination of action by all the partners.

Let us also note the following circumstance. When a firm raises its prices, this act does not directly express (in contrast to lowering prices) an aggressive strategy designed to recarve the market: if its rivals do not use this step for a concerted increase of prices, the former can always retreat to its initial position. This produces the most frequent probing by individual oligopoly firms of the possibility for raising prices. So, price leadership is realised more easily in raising prices than in lowering them. Some empirical studies of the interaction between individual prices of the major corporations bear this out: in recent decades, there has been much more concerted action in raising prices than in lowering them.[1]

Let us now consider wage inflation. Many advocates of this theory try to take the trade union issue out of the general economic context, regarding their activity as being simply arbitrary in a "permissive" situation. They believe that the actual growth of labour productivity should be the ceiling for wages. That is why some suggest as the main criterion to single out cost inflation the ratio between wages and labour productivity, for, they say, a faster growth of nominal wages as compared with labour productivity shows that price growth

[1] See: George Stigler, "The Kinky Oligopoly Demand Curve and Rigid Prices". In: *The Journal of Political Economy*, Vol. LV, October 1947, No. 5, pp. 432-449; R. Lonzilotti, "Competitive Price Leadership—A Critique of Price Leadership Models". In: *The Review of Economics and Statistics*, February 1957; Walter J. Primeaux, and Mark R. Bomball, "A Reexamination of the Kinky Oligopoly Demand Curve". In: *The Journal of Political Economy*, Vol. 82, No. 4, July-August 1974, pp. 851-862.

has been caused by the working-class struggle for higher wages.[1]

But labour productivity and wages (in other words, unit labour costs) in fact have no "rigid" relation with the price level. Between them there is always a number of intermediate elements (the nature of the distribution of newly created value, primarily, the relation between the movement of wages and profits; changing efficiency indicators in the use of fixed capital, raw and other materials, etc.). Periods may always be traced in the history of the capitalist countries when the faster growth of wages as compared with labour productivity is not attended by a growth in the general price level or, conversely, when the consumer price index grows while wages lag behind labour productivity. Thus, in the second half of the 1960s, nominal wage rates of Japanese workers grew at roughly the same rate as labour productivity, but this did not prevent the consumer price index from going up by nearly one-third over a period of five years. In the United States, unit labour costs gradually declined between 1961 and 1965, while the rate of profit increased from 16.7 per cent to 21.9 per cent); meanwhile, the wholesale price index for manufactured goods slightly increased.[2]

Let us assume, however, that over this or that period wages tended to increase faster than labour productivity, while the consumer price index grew. Does that warrant the conclusion that inflation was ultimately caused by a "much too rapid" growth of wages? Such a conclusion is ab-

[1] See, for example, Gottfried Haberler, *Inflation. Its Causes and Cures*, American Enterprise Association, Washington, 1960, p. 23; Howard S. Ellis, "The Effects of Post-War Inflation". In: *Inflation*, Proceedings of a Conference held by the International Economic Association, London, Macmillan & Co., New York, 1962, p. 67.

[2] *The Labour Market and Inflation. Proceedings of a Symposium held at Geneva by the International Institute for Labour Studies*, Macmillan, London, 1968, p. 37.

solutely unwarranted. Any price growth, and above all a growth of prices caused by vast military expenditures inevitably leads to an accelerated growth in wages as compared with labour productivity.[1]

Here is a simple example. Let us assume that, as a result of a sharp expansion of money demand caused by the arms race and deficit financing,

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[1] Indeed, a growth of prices implies that the national income in current prices has been growing faster than in constant prices, or

$$\frac{Y_1}{Y_0} : \frac{Y_1'}{Y_0'} > 1, \tag{1}$$

where Y_1 and Y_0 are, respectively, the final and initial levels of the national income expressed in current prices, while Y_1' and Y_0' are the final and initial physical volumes of the national income.

Let us note that

$$Y_1 = Y_0 \left[(1-\pi)\tau_1 + \pi\tau_2\right] \tag{2}$$

where τ_1 is the wage growth rate, τ_2 the growth of the other incomes, and π the initial share of incomes (not relating to wages) in the national income. Instead of Y_1'/Y_0', the growth of labour productivity indicator θ can be used in the first approximation:

$$\frac{Y_0'}{Y_0'} = \theta. \tag{3}$$

Let us substitute (2) and (3) in the expression (1), to obtain:

$$\frac{\tau_1}{\theta} + \frac{\pi(\tau_2 - \tau_1)}{\theta} > 1.$$

Consequently, if the share of the working class in the national income is not to decline, i.e., $\tau_1 \geqslant \tau_2$, nominal wages, regardless of the causes of the growing consumer price index, must increase faster than labour productivity. Moreover, when inflation is intense, the share of wages in the national income may shrink despite the faster growth of wages in the national income as compared with labour productivity. Let us assume that prices and labour productivity have gone up by 4 per cent, and incomes, not relating to wages, (i.e., profit in the first place), by 10 per cent. Then with π equal to, say, 0.5, this will mean an increase in nominal wages by 6 per cent, i.e. wages will grow much faster than labour productivity, but their share in the national income will decline from 50 per cent to 49 per cent.

prices over a year have increased by more than 3-3.5 per cent (figures which roughly correspond to the average rate of labour productivity growth in the United States). Then, in order to prevent a decline in real wages and, given a considerable rate of price growth, also to prevent the drop in workers' real incomes from being too great, nominal wages need to increase faster than labour productivity. It is not surprising, therefore, that in the conditions of "hyperinflation" caused by the gigantic growth of military and other government outlays, nominal wages have been growing much faster than labour productivity.

The cost inflation concept has clearly revealed the ongoing modification of theoretical concepts in bourgeois economics. The monetarist concept of inflation started from the assumption that price formation was entirely regulated by free competition between sellers and buyers. But Keynes's theoretical system assumed an insufficient flexibility of prices, at any rate, for some production factors, but with overproduction and "underemployment" this could sooner be manifested in a slow reduction or even stability of "unit costs".

In the recent period, there has been an incipient shift in the elaboration of theoretical price formation schemes: price movement models based on an unconstrained functioning of competitive forces have been losing popularity, as the following characteristic example shows.

Not long ago John Hicks was justly regarded as one of the most consistent and serious advocates of the postulate of perfect competition and flexible prices. In a book written in 1939 he says that abandonment of the assumption of perfect competition will inevitably lead to a collapse of a larger part of economic theory.[1] Not much time has elapsed

[1] John Hicks, *Value and Capital*, Clarendon Press, Oxford, 1939, p. 84.

since then. But today, after a series of scandalous anti-trust investigations in the industrialised capitalist countries, and the upheavals of the 1970s on the world markets, we find that Hicks has noticeably changed his tone. He has now introduced the concept of "fixprice markets" on which prices are directly fixed by the owners of goods; the level of these prices is influenced, alongside demand and supply, by a number of other factors. The unorganised "flexprice markets" of the old type have been gradually disappearing. The fact that the new markets are mainly inflexible price markets hardly needs to be specially verified, for this will be established by the most ordinary observation, Hicks said in 1977. Further on he referred to monopoly trends which are visibly manifested on so many of these markets, as exemplified by the oil cartel.[1] This "reappraisal of values" in the general approach to analysing market equilibrium and of the postulates of microeconomic analysis necessarily had an effect on the new theoretical concepts of inflation.

In the light of this, it is highly indicative that the "new inflation" concept has to refer quite openly to the role of oligopoly and monopoly practices in price formation in the current rise of the consumer price index. Its initial premises are directly connected with the theory of so-called imperfect competition.

However, price regulation is reflected and recorded by the new concepts of inflation in an irrational form. The relations in oligopoly price formation are presented in the form in which they can be observed on the surface of market relations in the capitalist world today.

The point is that every demand for higher nominal wages made by unionised working people is usually at once broadly publicised. As the strike movement

[1] John Hicks, *Economic Perspectives. Further Essays on Money and Growth*, Clarendon Press, Oxford, 1977, p. XI, 107.

in support of this demand gathers momentum (and in some cases the outcome of the ongoing struggle is also made contingent on decisions taken at government level), the whole of society is set in motion, with the mass media increasingly concentrating on the intense class conflict. Meanwhile, there is no noise over the unilateral decisions by Big Business to raise prices in a favourable market situation, with the price changes initially assuming covert forms and the resultant increase in capitalist profits divided among entries into various items of the balance-sheet.

All of this has apparently helped to spread the bourgeois apologetic concepts which ignore the independent and active role of monopoly price formation and which link the main changes in the system of prices and incomes only with workers' demands for higher wages.

It is true that with the growth of inflation public attention is being drawn to the pricing policy of the biggest companies, and from time to time the governments of some capitalist countries have to put ceilings on price increases by some companies, and in some cases the activity of anti-trust agencies is invigorated.[1]

In these conditions, Big Business has to modify its economic strategy: the most powerful corporations seek to time every noticeable price increase to coincide with the conclusion of new collective bargaining agreements and press reports about increases in nominal wages. An increase in costs, especially wages, where it is broadly publicised, is regarded as the best justification for raising prices.[2] In recent years, announcements of price

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[1] Thus, in the United States, the number of anti-trust trials involving big corporations and heard by the Federal Court went up from 420 in 1961 to 1,379 in 1972. (*Fortune*, April 1973, p. 64.)

[2] *Price Policies and Practices. A Source Book in Readings*, Wiley, New York, 1967.

rises by the major corporations in the automobile and other highly concentrated industries in the United States were most frequently timed to coincide with the end of strikes for higher wages.[1]

This timing also proves to be the best from the standpoint of price leadership: the renegotiation of the terms of collective agreements is a peculiar signal for the major corporations engaged in monopoly coordination of action aimed to hike prices. This is especially true for the concentrated industries where corporations, at that moment, have no secret or public aggreements directly regulating prices. At the same time, the renegotiation of collective agreements is also an important element in the well-geared system of monopoly coordination. In recent years, US steel companies have habitually announced general price changes to coincide with the completion of the annual wage changes.[2] Here is a characteristic exchange between a Senator and the President of the US Steel Corporation at a Congressional hearing on "regulated" prices:

> "*Senator Kefauver*. You say you didn't consult with them (with other entrepreneurs—*R.E.*) ... but it is a fact that substantially they followed your prices. You don't deny that, do you, Mr. Blough?
>
> *Mr. Blough*. I would say that possibly one of the reasons that was going through their minds, ... was the fact that we have a substantially uniform labor contract in the steel industry, and I suspect that their cost

[1] See: J. Lang, T. Nakayama, "The Anatomy of Price Change in 1970". In: *Monthly Labor Review*, February 1971, p. 41.

[2] *Frequency of Change in Wholesale Prices. A Study of Price Flexibility. A Study Prepared for the Joint Economic Committee by the United States Department of Labor, Bureau of Labor Statistics*, Government Printing Office, Washington, 1959, p. 7.

> increases were going up at somewhat the same rate that ours were going up."[1]

In other words, changes in labour costs at once set in motion the mechanism of monopoly coordination by the big firms, so bringing about a further increase in market prices.

It is especially important to bear the following point in mind: in many instances, a relatively small wage increase provides the pretext for price hikes. One US journal wrote: "Had there been no wage advance steel prices would have gone up substantially anyway."[2] No wonder, the increases in the price of steel are always well ahead of the growth of unit labour costs. When raising prices, corporations usually increase the amount of additional costs by 100-150 per cent.[3]

In other capitalist countries (e.g., the FRG), says Herald Scherf, the employer

> "seeking to avoid undesirable public pressure, provides himself with an 'alibi' by synchronising the increase in prices with the growth of wages... As a result, public opinion is being clearly induced to accept the idea of 'rising costs', so as to justify the 'forced' price adjustment."[4]

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[1] *Administered Prices. Hearings before the Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary United States Senate. 85 Congress, 1st Session*, Government Printing Office, Washington, 1958, p. 231.

[2] *Iron Age*, Vol. 162, No. 6, August 5, 1948, p. 119.

[3] See: *Business Week*, August 11, 1956, No. 1406, pp. 24-25. So, in 1956 and 1957, unit labour costs per tonne of steel went up by an average of $ 2.50-3.00, and the price of a tonne of steel by $ 6. (*The Relationship of Prices to Economic Stability and Growth. Commentaries*, Washington, 1958, p. 21.)

[4] Herald Scherf, *Untersuchungen zur Theorie der Inflation*, J. C. B. Mohr (Paul Siebeck), Tübingen, 1967, p. 74; Horst Georg Koblitz, *Einkommensverteilung und Inflation in kurzfristiger Analyse*, Walter de Gruyter, Berlin, 1971, p. 68.

This in a sense completes the process of fetishisation of the relations arising from the monopoly interaction between prices and costs, notably, wages. One is left with the impression that the growth of costs, including nominal wages, always provides the initial impetus and is the sole cause behind current inflation.

Under free competition, the capitalist class was able only as an exception, in special "local" conditions, to

> "avail itself of every rise in wages in order to raise prices of commodities much higher yet and thus pocket greater profits".[1]

These practices are much more widespread now that the price of labour power, like the prices of most other commodities, is subject to private-monopoly and state-monopoly regulation. But the ungoverned forces of the capitalist market themselves generate the trend to the faster growth of prices.

Let us consider, for instance, the ratio taking shape between prices and wages in the phase of cyclical boom, i.e. a period when the main increase in nominal wages occurs. An analysis of the movement of prices and wages not only among monopoly corporations but in industry as a whole shows that cyclical increases in nominal wages usually follow, with a short lag, the growth of prices, instead of outstripping it. The share of profit in the price of commodities is increased very much earlier.[2] Calculations show an especially noticeable lag in the

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[1] Karl Marx, *Capital*, Vol. II, Progress Publishers, Moscow, 1971, p. 344.

[2] See: Daniel Creamer, "Behavior of the Wage Rates During Business Cycles", *Occasional Paper 34*, National Bureau of Economic Research, New York, 1950; C. D. Long, "The Illusion of Wage Rigidity: Long and Short Cycles in Wages and Labor". In: *The Review of Economics and Statistics*, Vol. XLII, May 1960, No. 2, pp. 140-151; Edwin Kuh, *Profits, Profit Markups, and Productivity. An Examination of Corporate Behavior since 1947*, Government Printing Office, Washington, 1960.

cyclical increase in wage costs. Consequently, the increase in wage costs in the phase of cyclical upswing most frequently turns out to be the result of higher prices. Geoffrey H. Moore, one of the best-known US analysts of the cycle, writes:

> "Rates of increase in hourly compensation ... are usually at a moderate level during the initial phase of the upswing in prices, but soon begin to rise, partly in response to the price movement."[1]

At the same time, an analysis of the time series characterising wage rates and prices over a long period by means of modern mathematical methods (spectral analysis, etc.) will also testify that the rise in prices, as a rule, precedes the growth of wages.[2]

Today, with the steady growth in the consumer price index, the struggle for higher wages is above all a protective response by the working class to the sustained offensive by the monopolies against its vital rights.[3]

At the same time, the price increases by the monopolies are, as a rule, very much in excess of the wage costs. Otto Eckstein, who made a detailed analysis of the causes behind the increase in prices

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[1] Geoffrey H. Moore, "The Cyclical Behavior of Prices". In: *The Business Cycle Today*, Columbia University Press, New York, 1972, p. 161.

[2] Thus, making use of the Simms criterion for annual data characterising the movement of prices and hourly earnings in the US manufacturing industry since the First World War and also similar quarterly data over the postwar period, one can establish (naturally within the framework of the definitions used by this criterion) a one-sided causal relationship: price changes lead to wage changes.

[3] "A voluntary abstention from wage-raise demands by one particular union will do little to relieve the overall inflationary pressure, and will indeed put its members completely at the mercy of rising prices." (William J. Baumol, *Welfare Economics and the Theory of the State*, Harvard University Press, Cambridge, 1965, p. 141.)

from 1955 to 1957, reached the following conclusion: "The data do suggest that the wage-price spiral does not fully explain the inflation by any means."[1] Statistical analysis shows that the growth of prices in the postwar years has not only fully covered the increase in wage costs, but has also enabled businessmen further to boost their profits.

The rapid growth of inflation explodes the idea that the growth of prices is caused by an "excessive" increase in wages. Thus, in many capitalist countries the especially rapid growth of the cost of living in the late 1960s and early 1970s was accompanied with a steady decline in the share of wages in the net value of the product of industrial firms and a sharp slowdown in the growth of the working people's real incomes, and frequently even with an absolute reduction of their incomes.[2] Recent statistical data show very well that wage rises lagged behind price increases in time, and in many instances, in scale as well, which shows that the current inflation has operated as the key instrument in the redistribution of the national income at the expense of the working class.

While summing up what has been said above, one must note that it is the state-monopoly structure of present-day capitalism itself that produces forms of price-cost interaction in which the growth of costs leads to an increase in prices. This interaction is a key element of the economic mechanism of present-day inflation. Because of it (and also of some other elements of this mechanism) any price increase, including, say, the cyclical growth of prices for capital goods, soaring prices for the goods turned

[1] Otto Eckstein, "Inflation, the Wage-Price Spiral and Economic Growth". In: *The Relationship of Prices to Economic Stability and Growth*, p. 371.

[2] In the United States, the share of wages in the net value of the product of non-financial corporations steadily shrank over the first half of the 1970s, and in 1973-74 there was a trend towards a reduction in real family earnings of US working people as well.

out in some industries involved in a restructuring of the economy, etc., could produce a cumulative buildup of the inflationary process.

4. The Phillips Curve

Let us recall that the concept of inflation set forth by Keynes in his *General Theory* was formed under the influence of a deep economic crisis and mass unemployment, which is why from the outset it was connected with his theory of employment. The further development of such concepts—as inflation became a more acute problem while the scale of unemployment declined as compared with the inter-war period—inevitably brought to the fore the correlation between the rate of general price rises and the scale of unemployment. Soon, the opponents of Keynesianism and other academic theorists actively joined in the discussion.

It was the British economist A. W. Phillips who examined the long-term and stable relation between unemployment and inflation. In an article[1] published in 1958 he suggested that there was a stable dependence of wages on the degree of unemployment, while the rate of wage growth so established, for its part, had a crucial influence on the pace of inflation. He considered the r lation between the share of unemployed in the total active population in Britain, on the one hand, and hourly wage rates and the consumer price index, on the other, over a period of nearly a century (1861-1957). The negative relation between these magnitudes was explicitly non-linear. As unemployment increased, there was a gradual decline in the rate of wage and price growth; at a certain level of unemployment (roughly

[1] A. W. Phillips, "The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861-1957". In: *Economica*, Vol. XXV, No. 100, November 1958, pp. 283-299.

5.5 per cent of the total labour force, according to the author) the growth of wages turns out to be completely paralysed, so that any further increase in unemployment must result in deflation, i.e. a drop in the absolute level of wages and prices. On the other hand, when unemployment is relatively small (in this case, short of 2.5-3 per cent of the labour force) there is usually a growth of wages and prices, and the rate of inflation must grow with the decrease in unemployment.

This article soon came to be seen as a "classical work", and Tobin said that it was the most influential macroeconomic work of the past quarter-century.[1]

However, it is not so easy to understand the reasons for this enthusiasm. The idea of a negative relation between the rate of inflation and the growth of unemployment was expressed long before Phillips's article, and in the preceding period some statistical calculations were published to show this relation.[2] The idea that there was a stable relation between the growth of the general price level and the rate of unemployment could have appeared especially important in the late 1950s and early 1960s, because that period dispelled the last doubts concerning the chronic nature of postwar inflation, and there was a feverish search for the causes of the growing consumer price index. Some Keynesians who saw this relation as the missing link (price equation) in the neo-Keynesian macroeconomic theory were especially active in elaborating Phillips's scheme.

Phillips did not give any theoretical explanations

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[1] J. Tobin: "Inflation and Unemployment". In: *The American Economic Review*, March 1972, p. 4.

[2] Characteristically, in the 1970s, a leading US journalist reprinted an article published by Irving Fisher back in 1926 and entitled "A Statistical Relation Between Unemployment and Price Changes". In: *International Labour Review*, Vol. XIII, No. 6, June 1926, pp. 785-792.

concerning the non-linear relation between inflation and unemployment, but he used aggregated data on unemployment, wages and prices, ignoring any possible structural effects. He did not examine, for instance, the question of the simple meaning of the aggregated function within the changing distribution of unemployment between individual industries.

This idea was further elaborated by Richard G. Lipsey in 1960.[1] He postulated a relation between the rate of change of money wage rates and demand on the labour market (he uses unemployment data to characterise such a statistically unobservable magnitude as excess demand for labour). In every industry, the greater the excess demand for labour, that is, the smaller the scale of unemployment, the greater the rise in wages. If this relation is non-linear on at least one of the labour markets, the weighted average of the individual functions will be shifted downward as compared with the aggregate function, and the shift depends on the degree of unevenness in the distribution of unemployment among the individual industries. In that case, when the parameters of the Phillips curve are assessed, the response of wages to the growth of excess demand for labour will turn out to be overstated, and the response of wages to shrinking demand, understated.

The point at which the excess labour demand-curve intersects with the abscissa axis should, in accordance with these assumptions, characterise unemployment, which remains even when the excess demand for labour disappears (friction unemployment). What is it then that determines the scale of friction unemployment, i.e. unemployment which

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[1] Richard G. Lipsey, "The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom. 1862-1957: A Future Analysis". In: *Economica*, Vol. XXVII, No. 105, February 1960, pp. 1-31.

is compatible with the stability of money wages? Up to now, there is no coherent theory that could provide anything like a convincing answer to this question. Let us mention among the various approaches only the very fashionable attempts by the "new microeconomic theory" to connect the existence of friction unemployment with the imperfections of the mechanism of economic information, including incomplete information concerning the availability of vacancies. In such models, the scale of friction unemployment may be determined by the relation between the number of vacancies and the number of job-seekers.[1]

Such theoretical constructs link price changes with the growth of wages by means of the conventional assumptions according to which prices are formed on the basis of unit costs and a constant mark-up. This obscures the dependence of prices on other factors (like the other elements of costs and the amount of profit), bringing to the fore only the "universal relation" between unemployment and the pace of inflation.[2]

The Phillips doctrine soon became popular not only in academic circles, but also among politicians. From the second half of the 1960s on, virtually every document setting forth the economic strategy of the governments of the United States, Britain, and other industrialised capitalist countries mentioned an inverse proportion between the scale

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[1] See: Dale T. Mortensen, "Job Search, the Duration of Unemployment, and the Phillips Curve". In: *The American Economic Review*, December 1970, Vol. IX, No. 5, pp. 847-862; Bent Hansen, "Excess Demand, Unemployment, Vacancies, and Wages". In: *The Quarterly Journal of Economics*, Vol. LXXXIV, February 1970, No. 1, pp. 1-23.

[2] This also applies to the initial relation between unemployment and the growth of wages. "If the rate of wage change is proportional to the amount of excess demand which in turn is measured by unemployment, there is no room for other variables" (George L. Perry, *Unemployment, Money Wage Rates, and Inflation*, The M.I.T. Press, Cambridge, Mass., 1966, p. 22.

of unemployment and price rises.[1] In many West European countries and Japan, some said that with the existing "excessively low" level of unemployment inflation should be regarded as a normal and natural phenomenon.

But a number of the more conservative economists saw the Phillips doctrine as a convenient pretext for attacking the very principle of so-called full employment. It was frequently suggested that inflation could be stemmed only through a "larger average margin of an unused productive potential, and a higher average level of unemployment than those to which the postwar generation has become accustomed".[2] Other economists concluded that nothing much would be gained from another "experiment in sadism"[3] to squeeze inflationary expectations out of the economy.

Since the Phillips curve is, in effect, a kind of reduced form, it allows the most diverse theoretical interpretations of inflationary process and also various assumptions concerning the economic mechanism linking price growth rates with the state of the labour market.[4] That is why one will find any number of attempts to connect elements of the

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[1] Consider the following headings in the 1970 report produced by the Council of Economic Advisers under the US President: "Dilemma: unemployment or inflation", "The best alternative between unemployment and inflation", etc. (*Economic Report of the President Transmitted to the Congress, January 1970*, Washington, 1978).

[2] F. W. Paish, *Rise and Fall of Incomes Policy*, The Institute of Economic Affairs, London, 1969, p. 62.

[3] *Economic Policy and Inflation in the Sixties*, American Enterprise Institute for Public Policy Research, Washington, 1972, p. 63.

[4] Analysing the function of wages in Phillips' model, Keith B. Griffin remarked back in 1962: "The relationship is very loose... Thus the notion of the Phillips curve can be subjected to any interpretation one desires." (K. B. Griffin, "Note on Wages, Price and Unemployment". In: *Bulletin of the Oxford University Institute of Statistics*, Vol. 24, August 1962, No. 3, p. 383.)

Phillips curve with earlier views of inflation. One proposal was to use the employment-price relation as a criterion for singling out cost inflation.[1] Theoretical schemes were also worked out to include the Phillips curve as an element into the monetarist theory of inflation.

Still, the spread of models that included the Phillips curve marked a definite shift of accent in the views on inflation. The recognition that there was an objective relationship between the movement of wages and the level of unemployment cast doubt on the idea that the working people's "unbridled" and "excessive" demands for higher wages were the key factor in raising the consumer price index.

In place of the sole point of equilibrium which characterised a situation of "full employment" in the Keynesian schemes, the Phillips concept proposed a set of equilibrium situations. However, the content of the "economic equilibrium" concept also changed somewhat because it now included not only the existence of some unemployed, but a steady rise in the general level of prices (chronic inflation) as well.

The conclusion that over a long term unemployment and prices were in inverse proportion to each other reflected some features of the reality. The long-term growth of prices has always revealed the explicit influence of cyclical factors, and the level of unemployment is one of those indicators which sensitively reacts to fluctuations in the market situation. That is why in periods of cyclical upswing the level of unemployment tends to go down while the growth of prices accelerates, whereas the very opposite trends are observed in periods of crisis.

[1] Edmund S. Phelps wrote that "cost inflation" is a term that could be used to denote "that kind of inflation which can be stopped only by a reduction of the employment rate". (E. Phelps, "Money-Wage Dynamics and Labour-Market Equilibrium". In: *The Journal of Political Economy*, Vol. 76, No. 4, Part II, July-August 1968, pp. 680-681.)

This expresses only the most general and superficial relationships between various processes of reproduction, and not in any sense any special influence on prices on the part of the "magic" factor of unemployment. Curves like the Phillips curve can be obtained by correlating the rate of price growth and other coincident indicators characterising the development of the cycle, like the extent to which production capacities are used. But even this is not an unconditional uniformity: considering that cyclical expansion of production entails a rise in the general level of prices, one could assume that a shrinking of marketing outlets leads to an equally marked fall in prices. But this assumption is refuted by the entire record of postwar recessions.

The "unemployment or inflation" dilemma largely owes its popularity to the very elementary nature of these interrelationships and reasoning.[1] A closer analysis of the problem inevitably shows the serious weaknesses and contradictions in the formulation of the problem itself.

Like any general assertion operating with a relation between two highly aggregated variables, the Phillips principle is at best a very approximate one. Let us recall that his main contribution to macroeconomic theory was seen by his followers in the idea that there was a stable relation between the level of unemployment and the price rates, but the fact is that this relation is a reduced form which depends on a considerable number of structural parameters and is, for that reason, extremely unstable.[2]

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[1] Some writers have noted that the conclusion drawn by Phillips and his followers did nothing to change the system of generally accepted views, but merely clarified the "dilemma" problem as a whole. (Axel Leijonhufvud, "Comment: Is There a Meaningful Trade-off Between Inflation and Unemployment?" In: *The Journal of Political Economy*, Vol. 76, No. 4, Part II, July-August 1968, p. 738.)

[2] Thus, assessment of the Phillips curve for the United States in the late 1960s inevitably started from the economic structure, which was characterised by telling expenditures

Statistical calculations show, for instance, that in normal conditions, i.e. with unemployment not too high, wage changes turn out to depend more heavily (and in many cases, heavily) on changes in consumer prices than on the level of unemployment. From this it follows that a substantial speed-up of inflation could altogether shift the Phillips curve; in that case, price growth will be accompanied with a growth rather than a reduction of the share of unemployed in the total labour force, or in other words, the movement will proceed not *along* the curve, but from one curve to another. Such a situation becomes especially probable under so-called hyperinflation, when the rapid growth of prices has a noxious effect on the whole course of economic development, checking the growth of employment in the key sectors of the economy.

That is why the attempts to produce a quantitative value for unemployment that would safeguard the economy against inflation turned out to be so flimsy. In 1960, Samuelson and Solow proposed the use of the Phillips principle as a major instrument in choosing government economic strategy. They used US data to calculate the long-term relation between the level of unemployment and the rate of inflation. As a result, they reached the conclusion that 4-5 per cent growth of prices turned out to be possible only if the level of unemployment dropped to 3 per cent of the labour force.[1] But subsequent US economic development failed to bear out these forecasts, and it was discovered, once again, that very different price growth rates could correspond to the same level of unem-

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on the war in Vietnam. A switch of government spending to military purposes must inevitably lead to a shift in the Phillips curve. (See: L. Klein's comments in *Brookings Papers on Economic Activity*, Brooking Institution, Washington, 1970, No. 1, p. 47.)

[1] Paul A. Samuelson, Robert M. Solow, "Analytical Aspects of Anti-Inflation Policy". In: *The American Economic Review*, Vol. L, May 1960, No. 2, pp. 177-194.

ployment. The same thing happened to the prognostications of some other economists, who had fairly good results in adjusting the curve to the available points, but, as the inflationary process accelerated, the forecasting properties of models using the Phillips principle proved to be worse and worse. Once again economists had to face a situation in which large values of multiple determination coefficients (R^2) were not yet evidence of satisfactory forecasting properties of models because of the extreme instability of regression relations.[1] In many cases, analysts faced the above-mentioned situation—which could not be explained within the framework of the elementary Phillips concept—with a simultaneous increase in inflation rate and the share of unemployed in the able-bodied population.

Professor Robert J. Gordon carried out extensive statistical studies of the problems of price modelling and reached the following conclusion:

> "There is ... no permanent, stable trade-off between unemployment and inflation, as implied by the previous Phillips curve investigations."[2]

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[1] Having compared their forecasts of wage increases on the strength of the Phillips curve with the actual data, a group of British economists reached the following conclusion: "The orthodox 'Phillips'-type explanation simply does not apply" ("The Economic Situation: Annual Review". In: *National Institute Economic Review*, No. 55, February 1971, p. 40.) Albert Rees and Mary T. Hamilton noted that these relations largely depended on the choice of other parameters, methods of processing statistical data, etc. and added: "For this reason, the authors of Phillips curves would do well to label them conspicuously 'Unstable. Apply with extreme care'." (A. Rees, M. T. Hamilton, "The Wage-Price-Productivity Perplex." In: *The Journal of Political Economy*, Vol. 75, February 1967, No. 1, p. 70.)

[2] R. Gordon, "Problems in Predicting the Rate of Inflation". In: *Economics—A Half Century of Research 1920-1970, 50th Annual Report. National Bureau of Economic Research*, New York, 1970, p. 30.

In this situation, some economists, including Phelps and Friedman, proposed a new interpretation of the stability of the Phillips curve.[1] Thus, they draw a distinction between expected and unexpected changes in aggregate money demand. When the expansion of money demand unexpectedly accelerates, employers are guided by expectations of a subsequent sizable growth in the prices of their products and so are prepared to pay higher money wages to workers (from the employers' standpoint there may be a decline in real wages in terms of the new prices). On the other hand, workers associate increases in their nominal incomes with a growth of real wages. As a result, unemployment will temporarily decrease, but when the false expectations produced by the switch to the new expansion rate in nominal aggregate demand disappear, unemployment is bound to return to the old equilibrium level determined by real, and not monetary, factors.

So, it turns out that the exaggerated expectations of the economic agents are the only force which upsets the equilibrium of the whole economic system. In the subsequent period, the concept of "rational expectations" formulated in the early 1960s by J. Muth[2] was used for a new interpretation of the Phillips curve with the assumption that economic agents may be wrong in their expectations only over relatively short periods of time, whereupon they once again become "rational" and the old equilibrium level of unemployment is gradually restored.

The equilibrium rate of unemployment is usually designated as "natural", as Friedman does (by

[1] Edmund S. Phelps, "Phillips Curves, Expectations of Inflation and Optimal Unemployment Over Time". In: *Economica*, Vol. XXXIV, No. 135, August 1967, pp. 254-281; Milton Friedman, "The Role of Monetary Policy". In: The *American Economic Review*, March 1968, pp. 1-17.

[2] J. Muth, "Rational Expectations and the Theory of Price Movements". In: *Econometrica*, Vol. 29, No. 3, July 1961, pp. 315-335.

analogy with Wicksell's "natural interest rate", which is also determined by real factors). By definition, the "natural" level of unemployment is compatible with expected changes in aggregate money income and prices. Thus, in accordance with this concept there is no negative relation over the long term between unemployment and inflation (in other words, the long-term Phillips curve should be a vertical line intersecting with the abscissa axis at the point of the natural rate of unemployment). This returned the theory to the idea that there was a single point of stable equilibrium for a given period. But in contrast to elementary Keynesian schemes, this equilibrium situation was no longer connected with "full employment" of the whole labour force.

In Friedman's theoretical schemes, the vertical long-term Phillips curves were directly consonant with monetarist constructs. Thus, it turns out that the growth of money supply is the motive force of the process, but it cannot cause any long-term changes in the scale of employment (if the rate of unemployment was an equilibrium one at the initial moment); over the long term, it entails only an inflationary growth of prices.

At the same time, a somewhat different interpretation is put upon the traditional distinction between expected and unexpected inflationary processes. Consistently applying the idea of rational expectations, we are bound to reach the following conclusion: expected inflation cannot entail any dramatic perturbations in the real sector of the economy, and does not entail a burden for most economic agents. The only unfavourable effect of fully expected inflation should, in effect, prove to be a forced restructuring of assets implying a reduction in real money balances and their replacement with undepreciating material assets. Quite clearly, given this view there should be no serious apprehensions over the effects of inflation.

Let us also note that the merger of the new interpretation of the Phillips curves with the more general monetarist constructs substantially altered the accent towards the operation of cause-and-effect relations. The traditional Phillips principle was most frequently used to deduce the acceleration of the inflationary process from a shrinking in the rate of the unemployed in the total labour force or to suggest that inflation could be contained only by an increase in the scale of unemployment. In the new version, the vertical Phillips curves were used to illustrate the active role of the changes in aggregate money demand (and together with it, the changes in expected prices) which entail short-term changes in employment and output. Here, however, the inflationary process itself, or rather, the growth of prices which turned out to be unexpected leads to a temporary fall in unemployment.

The natural rate of unemployment is, in effect, a question that has no direct bearing on the government's current economic strategy. So long as wages respond to changes in current supply and demand, equilibrium on the commodity and labour markets will eventually be established on that level through the workings of the economic forces of "self-regulation". This approach indirectly reflects the more general notions propounded by Friedman and other advocates of this concept concerning the role the government has to play in the operation of the economic mechanism as a whole.

The schemes using the postulates of "new microeconomic theory" retain the same direction of the cause-and-effect relation.[1] In such constructs, the location of the Phillips curve is determined by the

[1] A theoretical analysis of the relation between the labour market and inflation will be found in the work by R. Lucas, L. Rapping, "Real Wages, Employment, and Inflation". In: *Microeconomic Foundations of Employment and Inflation Theory*, by Edmund Phelps et al., W. W. Norton & Co., New York, 1970.

response of factory and office workers to an increase or decrease in money wages. Thus, in the event of a reduction in wages, more and more workers will leave their employers in search of new vacancies that would help to maintain or raise thair wages. It will be easily seen that this reasoning involves only those who willingly leave their jobs, and this presents unemployment as a whole as a purely "friction" phenomenon. As for so-called forced unemployment, which is the gravest economic and social problem, it does not figure in such schemes at all. In addition, the advocates of "new microeconomic theory" lay special emphasis on the factors of uncertainty and costs incidental to the obtaining of information concerning available vacancies and wages. But in real life the system of modern communications reduces these factors to a secondary role, and this tends to make such models even less realistic.

Even when we confine ourselves to examining "voluntary" unemployment, the theoretical constructs of Lucas, Rapping and other advocates of "new microeconomic theory" can hardly be squared with the results of empirical observations.

Indeed, even the most cursory acquaintance with the concrete data will show that in real life the percentage of voluntary job-leavers reveals an explicit cyclical dynamic: as a rule, it tends to drop in the phase of recession, and markedly to increase in periods of economic revival and subsequent boom. But the premises of "new microeconomic theory" suggest that the movement of total unemployment should show the very opposite, anticyclical trends.

The introduction of an additional variable—expected prices—helps to tone down the idea that over the short run the relation between the rate of unemployment and the pace of inflation should be a rigid one. However, even these assumptions do not make much difference.

Let us consider, for instance, situations when it was impossible entirely to anticipate actual price growth and/or realise the inflationary expectations in a corresponding increase in wages. With such a price increase, the unemployment rate should, in accordance with the assumptions made by Friedman, Phelps and Lucas-Rapping, remain below the natural rate. On the other hand, when the actual unemployment rate is above the natural rate, all other conditions being equal, there should be a slowdown in the inflationary process. However, if one is entitled to associate the natural rate with the rate of unemployment which remains fairly stable over a long period (how can one otherwise empirically determine this magnitude which is so important for this concept?) one should reach the conclusion that the modified view of the Phillips curve does not accord with many episodes in capitalist development either.

Thus, econometric studies of the factors which determine the movement of wages in the United States and Britain show that up until the early 1970s in the administration of wages the coefficient of the variable characterising the movement of consumer prices always turned out to be smaller than unity.[1] There is no doubt that, say, from 1951 to 1961, the actual growth of prices in the United States, all other conditions being equal, could not have been fully realised in a corresponding increase of wages. Still, over that period, there was an

[1] J. Dow, L. Dicks-Mireaux, "The Determinants of Wage Inflation: United Kingdom, 1946-1956". In: *The Journal of Royal Statistical Society*, Series A., 1959, Part 2; L. R. Klein, R. J. Ball, "Some Econometrics of the Determination of Absolute Prices and Wages". In: *The Economic Journal*, Vol. LXIX, No. 275, September 1959, pp. 465-482; R. Bodkin, *The Wage-Price-Productivity Nexus*, Philadelphia, 1966; G. Perry, "Changing Labor Markets and Inflation". In: *Brookings Papers on Economic Activity*, No. 3, 1970; M. Sumner, "Aggregate Demand, Price Expectations and the Phillips Curve". In: *Incomes Policy and Inflation*, Manchester University Press, 1972, pp. 163-181.

upward trend in the unemployment rate, while the average length of unemployment period tended clearly to grow. Nor have the hypotheses of "rational expectations" been borne out by the calculation of prices in accordance with economic models (best known of which are those of Solow, Gordon, and Hymens). Under the influence of this criticism, some monetarists had to admit that "fully anticipated" inflation could hardly ever have been discovered in the real world, and are now prepared to stand up for the concept only as an instrument in abstract theoretical analysis.

Let us now turn to situations when the unemployment rate is clearly higher than the natural rate. Hardly any advocate of this concept will deny the fact that such a situation did arise in many capitalist countries as a result of the 1929-33 depression, when there was a sharp increase not only in the absolute but also in the relative scale of unemployment. Still, since 1933, it has been impossible to discover either in the United States or in many other capitalist countries any sign of accelerated deflation, or anything like a stable trend towards lower prices owing to the "excessive" unemployment. Attempts to explain the relation between money supply and employment or wages and employment over that period in models consistent with the Friedman-Phelps schemes proved to be futile.[1]

One could also refer to recent events. In 1976 and 1977, the unemployment rate in the United States was well above the average level of the preceding period, nonetheless since 1976 the inflationary process has tended to accelerate.

Let us also note the following. The use of the Phillips curve in combination with the "rational

[1] See, for instance, the report of a discussion at Rochester University in 1978, and also Robert E. Lucas, Leonard A. Rapping, "Unemployment in the Great Depression: Is There a Full Explanation?" In: *The Journal of Political Economy*, Vol. 80, No. 1, January-February 1972, pp. 186-191.

expectations" postulate inevitably leads to the conclusion that a rate of unemployment natural for the given economy (with slight fluctuations) should be maintained over more or less lengthy periods. But the events of the 1930s and the subsequent decades clearly testify not only to the continuous and marked fluctuations in unemployment but also to the fact that massive unemployment, once it has emerged, can remain at critical levels over fairly lengthy periods. Some of those who propound this view make the reservation that the natural rate of unemployment itself can change. But from this it follows directly that such changes should also be very long-term, for if relatively short periods are examined, the whole Friedman-Phelps scheme can remain meaningful only if the natural rate of unemployment remains unchanged.[1]

In the recent period, some economists (Modigliani and Papademus, Gordon, Wachter, among others) have tried to determine the numerical value of the natural rate of unemployment, or of the "non-inflationary" rate, as Modigliani and Papademus have called it, and discovered that it has a tendency steadily to rise. Thus, in the mid-1970s, in the United States, it came to roughly 5.5 per cent, whereas in the mid-1950s, according to Gordon, it stood at roughly 4 per cent, and during the cyclical upswing of the 1960s, according to Wachter, it was already over 5 per cent of the labour force.[2]

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[1] In an ironic commentary on the concept which allowed the possibility for such leaps and bounds in the natural rate of unemployment, Modigliani says: "What happened to the United States in the 1930s was a severe attack of contagious laziness". (F. Modigliani, "The Monetarist Controversy, or Should We Forsake Stabilisation Policies?" In: *The American Economic Review*, March 1977, p. 6.)

[2] See: F. Modigliani, L. Papademus, "Targets for Monetary Policy in the Coming Years". In: *The Brookings Papers on Economic Activity*, 1975, No. 1, pp. 141-165; R. J. Gordon, "Structural Unemployment and the Productivity of Women". In: *Stabilisation of the Domestic and International Economy*, Amsterdam, 1977, pp. 181-229; M. Wachter, "The Changing

Let us note at this point that the operation of the factors which determine the natural rate of unemployment and its long-term dynamics goes well beyond the limits of current economic changes. Thus, according to Friedman, this rate tends to rise in connection with the existence of minimum wage-rate laws and the power of trade unions.[1]

In other words, whereas the advocates of cost

Cyclical Responsiveness of Wage Inflation". In: *The Brookings Papers on Economic Activity*, 1976, No. 1, pp. 115-159.

[1] See, for instance, M. Friedman, "The Role of Monetary Policy". In: *The American Economic Review*, March 1968, pp. 1-17.

In his Nobel lecture, Friedman altogether cast doubt on the idea that unemployment is a form of inefficient use of resources on the plea that "a highly static rigid economy may have a fixed place for everyone whereas a dynamic, highly progressive economy, which offers everchanging opportunities and fosters flexibility, may have a high natural rate of unemployment". (Milton Friedman, "Nobel Lecture: Inflation and Unemployment". In: *The Journal of Political Economy*, Vol. 85, No. 3, June 1977, p. 459.)

Without going into a discussion of this highly dubious line of argument, which is designed somehow to justify the high level of unemployment, let us merely remark that the above-mentioned cases of a stable increase in the unemployment rate can hardly be tied in with the growing dynamism of the US economy: in these periods there was rather a lowering of the economic growth rate, and a slowdown in the growth of efficiency in the use of labour and material resources. But one can also refer to a number of calculations showing (however tentatively) a substantial (non-linear) increase in the efficiency of the use of material and labour resources with a reduction of unemployment. Thus, in accordance with the well-known Okun's Law, a 1 per cent reduction in the number of unemployed in the United States must now entail a 3 per cent increase in real GNP (this "Law" was initially formulated by A. Okun in his article, "Potential GNP: Its Measurement and Significance". In: *Proceedings of the Business and Economic Statistics Section*, Published by American Statistical Association, 1962, pp. 98-104). In accordance with Gordon's calculations, a temporary reduction in unemployment by one point in the early 1970s, had to have an increase in aggregate output by 2.3-2.7 per cent. (See: R. J. Gordon, "The Welfare Cost of Higher Unemployment". In: *The Brookings Papers on Economic Activity*, 1973, No. 1, pp. 162-164.)

inflation believe that trade union activity and increases in minimum wage rates are the most important source of inflation, Friedman says that it is caused by a growth of stable unemployment. The political conclusions from all these theoretical constructs appear to be highly transparent.

Let us note, finally, that the view of the unemployment-inflation relation is extremely limited in itself. Bourgeois economists and politicians point to the existence of a functional relation between growing unemployment and slower price growth, and usually put upon it a one-sided interpretation, claiming that the movement of unemployment is the prime cause behind all the changes in the movement of prices. Meanwhile with the state-monopoly structure of the economy, the opposite view is also well-substantiated; price movements can serve as an active factor of cyclical development also exerting an influence on demand for labour. For instance, the growth of prices during the economic crisis of 1973-75 gradually gathered momentum, despite the fact that effective demand in that period was rapidly shrinking. Price growth certainly induced greater underloading of capacities and more extensive unemployment.

5. Economic Theory and Anti-Inflationary Policy

The rapid rise in the general level of prices has an especially unfavourable impact on the country's balance of payments and the position of its currency on the money market. At the same time, the working people actively protest against a growing consumer price index and the constant threat of faster inflation. More and more sections of the population join in the fight for their vital rights, and this induces political leaders to make ever more frequent statements about the need to combat inflation. The task of keeping the national currency stable is now a key task of the government's economic policy.

The choice of instruments, of course, crucially depends on the overall politico-economic approach to the problem of inflation. Thus, the neoliberals claim that the growing socio-economic activity of the state is the chief cause of inflation. Wilhelm Röpke, a leader of this trend, said in his book that there was a democratic "social inflation" produced by the "ideology, forces and wishes of the modern mass democracy".[1] Moreover, inflation is connected with the general atmosphere of "permissiveness", which simultaneously produces explosions of student unrest, growing crime, etc.[2] Some neoliberals say that inflation is rooted in the social security system and in government spending under social and cultural programmes.[3]

What is also noteworthy is that the crisis upheavals of the 1970s, like the sharply intensified inflationary processes were directly or indirectly connected with sharp fluctuations in government activity. In these conditions, the monetarists have once again come forward with the idea that in present-day conditions the basic stability of the private sector tends to clash with the destabilising influence of the state sector. Such schemes, as a rule, claim that "government activism" and regulation policy based on the principles of "optimal control" are the basic source not only of inflation but of the general economic instability.[4]

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[1] Wilhelm Röpke. *Jenseits von Angebot und Nachfrage*, Eugen Rentsch Verlag, Erlenbach-Zurich, 1958, p. 256.

[2] See: R. Harrod, "The Issues: Five Views". In: *Inflation as a Global Problem*, Ed. by R. Hinshaw, John Hopkins University Press, Baltimore, 1972.

[3] See: A. Shonfield, "Welfare without Welfare State". In: *Il Politico*, 1966, No. 4, pp. 738-740.

[4] "Commentary on Monetary Economics: An Interview with Karl Brunner". In: *Review of Federal Reserve Bank of St. Louis*, November 1978, p. 9.

The monetarists say that the chief cause of the current inflation is the growth of the money supply stemming from the practice of the Keynesian principle of "full employment". Friedman claims: "Full employment policy is, however, a modern invention for producing inflation."[1] In the monetarist version of the Phillips curve, this idea is modified as follows: inflation is a product of government policy seeking to reduce unemployment below the "natural" rate. That is why the crucial instrument for combating inflation is, they claim, a sharp reduction in the sphere of government economic activity, notably, cuts in government spending and more rigid money and credit restrictions. Such programmes are most frequently extremely conservative: while advocating cutbacks in social insurance aid, appropriations for medical care and education, payments to small farmers, etc. the neoliberals stubbornly refuse to see one of the true sources of inflation, namely, the gigantic growth of militarism which involves military spending running to billions of dollars.

The neoclassics display no special enthusiasm for direct government control of prices and incomes.[2] The most consistent ideologists of this school believe that this expansion of the sphere of govern-

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[1] Milton Friedman, *Inflation. Causes and Consequences*, The Council for Economic Education, Bombay-New York, 1963, p. 9. In his Nobel Lecture, Friedman connected inflation not only with the principle of full employment but also with government social programmes: "Governments *have not produced* high inflation as a deliberate announced policy but as a consequence of other policies—in particular, policies of full employment and welfare-state policies raising government spending." (Milton Friedman, "Nobel Lecture: Inflation and Unemployment". In: *The Journal of Political Economy*, Vol. 85, No. 3, June 1977, p. 466.)

[2] Friedman, for instance, ironically remarks that since the period of Diocletian a government policy of regulating incomes has never succeeded in combatting inflation. But "when controls have been accompanied by sufficient monetary restraint, inflation has been stopped despite them". (*Newsweek*, December 22, Vol. LXXIV, No. 25, 1969, p. 48.)

ment regulation threatens gradually to paralyse the whole private-enterprise system. Hayek claims, for instance, that government regulation of prices will have a fatal effect on economic-activity incentives, and this will require even more intense "whipping up" of the economy by the government which, for its part, will further push up inflation, etc. In his view, this produces a "vicious circle" which leads the government into a system of overall controls and central planning.[1]

The neoclassics insist that the key anti-inflation measures should include a system of measures designed to reduce the sphere of government regulation and enhance the competitive principles in the development of the capitalist economy.[2]

The Keynesians take a slightly different view of the matter: during underemployment, measures aimed to stimulate the economy and involving an increase in money supply cannot lead to the development of inflation.

Here, the evolution of Keynes's own views is indicative. After the First World War, in the early 1920s, he kept emphatically pointing out all the dangers of government inflationary policy, but in the subsequent period, he seemed to have stopped noticing the unfavourable effects of the inflationary growth of prices caused by monetary and credit expansion, or the policy of deficit financing (the approach most actively propounded by Keynes in the latter half of the 1930s.)

In 1930, he wrote that the central bank can cope more easily with inflation than with a crisis drop

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[1] F. A. Hayek, *Studies in Philosophy, Politics and Economics*, Routledge & Kegan Paul, London, 1967, p. 276.

[2] See, for instance, F. A. Hayek, "Inflation, the Path to Unemployment". In: *Inflation: Causes, Consequences and Cures*, The Institute of Economic Affairs, London, 1974, pp. 115-120; F. Lutz, "Dilemmasituationen nationaler Antiinflationspolitik". In: *25 Jahre Marktwirtschaft in der Bundesrepublik Deutschland*, Gustav Fischer Verlag, Stuttgart, 1972, pp. 274-282.

in prices ("deflation"), although he continued to regard maintenance of the stability of the purchasing power of money as the "ideal goal" of monetary and credit regulation.[1] In his *General Theory* he makes no mention at all of the inflationary effects of government regulation.[2]

Keynes's refusal to discuss the prospect of developing inflation is apparently due not only to the above-examined methodology of Keynesian analysis, but also to the concrete historical conditions in which his doctrine was formulated. After all, a consistent development of Keynes's concept inevitably leads to the conclusion that government policy aimed at preventing inflation must restrain the expansion of effective demand, so increasing the scale of underloading of production capacity and unemployment. In the period of economic depression and with millions upon millions of unemployed, such recommendations clearly did the Keynesian theory little credit. Meanwhile, according to Hicks, Keynes acted as a prophet and propagandist, addressing himself to a broad spectrum of audiences.[3]

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[1] John Maynard Keynes, *A Treatise on Money*, Vol. II, pp. 163, 253.

[2] Lerner recalls: "In 1935 or 1936, Robert Bryce and I asked Keynes whether the maintenance of sufficient effective demand for full employment could not result in perpetuating inflation. Keynes could not understand our question, although we persisted until we exhausted his patience." (Abba P. Lerner, "Employment Theory and Employment Policy". In: *The American Economic Review*, Vol LVII, May 1967, No. 2, p. 2.) The situation appears to be especially paradoxical in view of the following circumstance: immediately upon the publication of the *General Theory*, some reviewers pointed out that with the strict observance of Keynes's theoretical assumptions employment could be maintained only through ever more intensive use of the printing press for the issue of money. (See, for instance, J. Viner, *The Quarterly Journal of Economics*, 1937, p. 149.)

[3] "He was selling his policy to politicians and public, by *Essays in Persuasion* and by newspaper articles galore. The *General Theory* was his way of selling his policy to professional economists." (J. Hicks, *Economic Perspectives. Further Essays on Money and Growth*, Oxford, 1977, p. 147.)

Keynes, like his followers, in that period wrote more frequently about the beneficial influences of "moderate inflation" on the development of the capitalist economy.

After the Second World War, some economists continued to hold that "mild inflation does at least some good".[1] But as the ever more numerous negative effects of the uncontrolled growth of prices began to come to light, the attitude to such growth began to change, and the assessments of inflation increasingly sounded like the groans of a heavy hangover. In the early 1970s, Lord Robbins remarked that "burning down the house to get roast pig" was a "rational operation" by comparison with the efforts to stimulate economic activity by means of inflation.[2]

In this situation, the spread of the Phillips concept, in effect, marked a further departure of the Keynesians from the idea of "full employment": after all, economic equilibrium characterised by a lower rate of price growth inevitably implied, in accordance with the Phillips scheme, a higher level of unemployment. Hence the very popular talk in the late 1960s and early 1970s about the "basic dilemma" of state regulation: the need to choose between unemployment and inflation.

The OECD McGracken group, including influential experts from eight countries, resolutely rejected the idea that the way out of the grave economic difficulties lay in promoting further inflation. They said that

> "recent experience has shown only too clearly how inflation tends to *feed on* itself... Accelerating inflation cannot be lived with, and,

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[1] *The American Economic Review*, Vol. XLVIII, September 1958, No. 4, p. 697.

[2] Lord Robbins, "Inflation: An International Problem". In: *Inflation as a Global Problem*, Ed. by Randall Hinshaw, The John Hopkins University Press, Baltimore and London, 1972, p. 13.

once it has begun, escape from it is far from painless."[1]

At the same time, the record of the price movements in the late 1960s and early 1970s induced some Western economists and political leaders to declare as inadequate all the indirect methods by means of which governments were trying to regulate prices. Many bourgeois economists believe that the "excessive" growth of "costs", above all wages, was the chief cause of the current inflation. Accordingly, the frankest recommendations boil down to a curtailment of the political rights of the most active contingents of the working people, the adoption of new anti-labour laws, and so on.

Chamberlin, for instance, says that all the measures of financial and credit policy are inadequate, so that the problem of inflation should be tackled on the level on which it arises, in other words, the government should take direct steps to curb the trade union struggle for higher wages: "Economists should be more vocal in their criticism of union power and tactics."[2] Moulton, another US economist, having examined the various recipes for controlling inflation, rejects all the earlier projects, with the exception of one: direct control over wages, asserting that the wage-bargaining table is the only effective point of control.[3] Some urge employers to unite and with the help of the government to display more firmness in fighting workers' demands for higher wages. Thus, in the intricate pattern of diverse socio-economic processes, the advocates of Big Business seek to identify and set apart the elements which could help to put the whole blame for the development of inflation on the workers.

[1] *Towards Full Employment and Price Stability*, OECD, Paris, June 1977, p. 18.

[2] Edward H. Chamberlin, "Labour Union Power and Cost-Inflation". In: *Inflation...*, p. 459.

[3] See: Harold G. Moulton, *Can Inflation Be Controlled?* George Allen & Unwin, London, 1958.

Let us consider, in conclusion, some of the practical results of anti-inflation regulation by the US Administration.

The speed-up of the inflationary process in the latter half of the 1960s was a direct outcome of the US government's escalation of military operations in Indochina. Thus, from 1965 to 1968, Federal purchases of goods and services for military purposes increased by more than 50 per cent, from $ 50.1 billion to $ 78.3 billion, while the monthly volume of prime contracts went up from $ 2.1 billion in early 1965 to $ 3.5 billion in mid-1966. Aggregate government and private spending was 3.1 per cent in 1964, 8.6 per cent in 1965, 12.8 per cent in 1966, and 15.1 per cent in 1968. This (and the effect of certain other factors) accelerated the growth of money supply: from 1965 to 1968, the aggregate M_1 went up by nearly 25 per cent. All of this increased tightness on many commodity markets and led to a rapid growth in the general price level. According to Eckstein's imitation with the use of a big econometric model, if it were not for the accelerated growth of military expenditures connected with the war in Vietnam, the wholesale price index in 1967 would have somewhat declined, and in 1968 increased by 0.6 per cent (actually, it grew by more than 2.5 per cent) and in 1969, by 2 per cent (as compared with the actual price increase of nearly 4 per cent).[1] Thus, the Democratic administration's policy of increasing government spending and maintaining credit and monetary expansion inevitably led to a sharp step-up in the inflationary processes.

The Republican Party's economic platform has long included the demand for keeping the purchasing power of the dollar stable. The eloquent tirades over the Democrats' neglect of the sufferings inflicted

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[1] O. Eckstein, *The Great Recession with a Postscript on Stagflation*, Amsterdam, 1978, pp. 26-29; *Economic Report of the President, 1973*, Washington, 1973, pp. 248, 275.

on the average American by the growth of prices, Johnson's high cost of living, etc., and mainly their assurances about a firm resolve to stop the growth of prices inevitably helped the Republicans to win the presidential elections in 1968 and 1972.[1]

Once installed, the Republican administration began to combat inflation in accordance with the monetarist recommendations. This was due above all to the Republicans' general stand in the political duel between the two bourgeois parties. The central plank of the Republican economic platform has always been that the government should intervene in economic life as little as possible so as to give full scope to "free enterprise". This is most in line with indirect methods of monetary regulation, which put fewer constraints on private-enterprise market relations than direct government regulation of the economy.

Economic experts testifying to the government and Congress in that period noted the advantages of monetary policy. Statements and hearings held by the Joint Congressional Economic Committee in 1967 showed that

> "a growing number of economists have come to downgrade the importance of fiscal policy as a determinant of economic activity. Instead, economists are increasingly impressed with the influence of monetary factors in shaping the course of economy."[2]

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[1] US public opinion polls show that in the early 1960s, the population was most alarmed over international political problems, but since the late 1960s and early 1970s, inflation and the growing cost of living have been the chief concerns. (See: William Watts and Lloyd A. Free, *State of the Nation, 1974*, Potomac Associates, Washington, D.C., 1974, pp. 20-22.)

[2] First National City Bank, *Monthly Economic Letter*, April 1967, p. 42. At the end of 1968, a subcommittee of the House of Representatives polled 71 experts on the desirable forms of economic regulation. Most of them opted

In 1969, following relevant consultations, the Federal Reserve Board adopted a number of decisions envisaging the introduction of monetary and credit restrictions. At the same time, there were cuts in some budget appropriations. These measures somewhat restrained the expansion of credit and money, so changing some of the general conditions in the country's economic development, but the results of this policy differed substantially from those the US Administration had expected.

The point is that by then the United States clearly revealed symptoms of another bout of overproduction, so that the government restrictions helped to start the economic crisis. Thus, using the terms of quantity theory, one could say that the restraint of growth (M) promoted a drop not in prices (P), but in current output (T). Meanwhile, the general level of prices continued to go up. In 1970 and 1971, even members of the administration had to admit that they had never expected a crisis recession on such a scale, or such small effects from deflationary policy.

By the early 1970s, the failure of the policy aimed at checking inflation became perfectly obvious. Despite some restraint on monetary expansion and the marked increase in unemployment and under-capacity of production, the inflation process continued to develop apace.[1]

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for a more vigorous monetary policy. (*Compendium on Monetary Policy, Guidelines and Federal Reserve Structure. Banking and Currency Subcommittee. House of Representatives*, Washington, 1968.)

[1] In 1967 the consumer price index went up by 2.8 per cent, in 1968 by 4.2 per cent, in 1969 by 5.4 per cent, and in 1970 by 5.9 per cent.

The inability of a government's anti-inflation policy to check the growth of prices or, at least, to prevent a speed-up of inflation induced some economists "with the sober realization that sharp and major changes in the rate of government expenditure for goods and services are likely to have effects which may not readily be counteracted, if at all, by the instruments of control ordinarily used. A $ 30 billion

These developments forced a marked turn in government policy. The advance of the crisis of overproduction forced the government to relax restrictions and then to resort to the usual Keynesian methods of stimulating the economy.

In those circumstances, other measures were required to limit inflation. Having gone back on all its earlier assurances about its desire to ensure a "free play of market forces", the Republican administration announced in the early 1970s that it was switching to a new "multiphase" economic policy providing at definite stages direct regulation of prices and wages. It is no part of this work to give a detailed description of each of the subsequent phases of regulation; let us merely note that the switch to a "new economic policy" clearly revealed the influence of the concept which linked up the development of inflation with an "excess" growth of "costs".

By the autumn of 1971, the Republican administration began to realise that the problem of inflation was so serious that, contrary to all its declarations about its unwillingness to "intervene" in any way in the operation of market processes, it resorted to methods of direct control over prices and wages. The restraint on the demands for higher money wages certainlv led to an accelerated growth of unearned incomes.[1] Meanwhile, even under official direct control over the prices of many goods it proved to be impossible completely to stop the growth of the consumer price index; besides, a large

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per year increase in defense expenditures plus withdrawal from the civilian labor force of a million or more men cannot be absorbed without corresponding cost in a full employment economy." (R. Eisner, "What Went Wrong?" In: *The Journal of Political Economy*, May-June 1971, pp. 639-640.)

[1] From 1970 to 1973, the wages paid to industrial workers and office employees by private US corporations dropped from 53.3 per cent of the national income to 51.8 per cent, while pre-tax corporate profits went up from 8.9 per cent to 10.8 per cent of the national income.

part of the "illegal" price increases simply could not be recorded by current statistics because of their covert forms.[1]

However, the effects of such regulation, which built up below the surface in the period of direct price and wage controls, had an especially big part to play, and moved into the foreground upon the completion of the phases of most rigid government regulation. The relaxation of government control in 1973 at once led to a sharp spurt in the inflation, so that phases III and IV of the anti-inflation policy could do nothing to prevent its development. Of course, the rapid growth in the general price level in 1973 and 1974 was connected with a number of specific exogenic factors, like the leap-frogging prices on the world market (notably the prices of energy resources and foodstuffs), the two devaluations of the dollar, etc. Still, most analysts believe that an extremely important factor behind the step-up in the inflation was the measures for "freezing" prices and wages and the subsequent lifting of these forms of regulation. Thus, according to some calculations (by Gordon and other US economists), the relaxation of government controls over prices and wages only in 1974 resulted in an additional growth of the consumer price index by at least 3 per cent.[2] What is more, neither those who make government policy, nor the authors of economic models were able to anticipate the opera-

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[1] A US weekly showed that the consumer price index continued to grow despite assurances of "control" allegedly guaranteeing price stability, and added: "Officials maintain that illegal price hikes have not been widespread, yet their own figures raise some doubt." (*Time*, November 15, 1971, pp. 30-31.)

[2] According to Eckstein's calculations, the lifting of controls over prices had the greatest effect on the movement of wholesale prices: throughout 1974 and 1975, their additional growth (connected only with the earlier forms of government regulation) came to over 3.5 per cent. (See: O. Eckstein, *The Great Recession with a Postscript on Stagflation*, North-Hall, Publ. Co., Amsterdam, 1978, p. 58.)

tion of these factors, which became patently evident in the manifest failure of the forecasts of price movements in the second and third quarters of 1974.

The following circumstance was also extremely important. The growing tendency towards synchronisation of inflation processes in the capitalist countries over the past few years has become a characteristic feature of their economic development. This is apparently due not only to the relatively more frequent coincidence of the phases of the economic cycle, but also to other forms of internationalisation of economic relations and the development of economic integration among these countries. The specific features of inflation as a global worldwide economic process characterising the development of the whole of the world capitalist economy have never been so pronounced as they are today. The operations of the multinational corporations, the intensified "export of inflation" to other countries, and especially the "explosion" of the raw material and food crises clearly demonstrated the limitations of the government anti-inflation regulation policy carried out on a national scale.

The more protracted and the faster the growth of the general price level, the more pronounced are the features of inflation as an ungovernable "self-moving" process. It is highly indicative that, despite the ever more active government policy of restrictions pursued from the end of the 1960s, the growth of prices accelerated, until it reached truly record, double-digit rates in most capitalist countries in the mid-1970s. Thus, in 1974, the cost of living in Japan went up by 23 per cent, in the United States by 12 per cent, in Britain by 16 per cent, in France by 14 per cent, and in Italy by 19 per cent. The sharp spurt of inflation once again helped to revive the monetarist concept and the vigorous advocacy of monetary restrictions as the main means of combatting the accelerating growth of prices.

The grave recession of 1974-75 and the marked decline in economic growth rates that followed resulted in a certain slowdown of the inflationary process. The subsequent revival of economic activity, however, once again made inflation an especially urgent problem. In 1977, the consumer price index went up by 6.8 per cent (as compared with 4.8 per cent in 1976), and the figure was even higher in 1978. Unemployment, which had gone down somewhat, also remained at an unprecedentedly high level (by the autumn of 1978, it came to roughly 6 per cent of the total labour force). In that situation, many economists had to admit unfavourable "shifts" in the Phillips curve.[1] There was a growing body of opinion that the discovered instability in the Phillips curve sharply reduced the possibilities of using it as a practical instrument of government policy.

Assumptions by economic agents concerning forthcoming price changes are especially important in contemporary models of inflation. The simultaneous growth of the unemployment rate and the speed-up of the inflationary process (upward shift in the Phillips curve) is now ascribed to the role of inflationary expectations, but the factors on which the shaping of these expectations depends have yet to be adequately clarified, and the indicators of inflationary expectations are most frequently indirect. The flimsiness of theoretical constructs in this sphere sharply limits the possibilities for their practical use as an instrument of anti-inflation

[1] Thus, Nordhaus, who in the spring of 1977, became a member of the Council of Economic Advisers under the US President, had written shortly before that as follows: "The dilemma for policymakers in choosing between inflation and output is not only cruel but becoming crueller. Indeed, the inability to control both inflation and unemployment within acceptable institutions is the major flaw of Western economics today." (William D. Nordhaus, "Inflation Theory and Policy". In: *The American Economic Review*, Vol. 66, May 1976, No. 2, p. 64.)

policy (to say nothing of the fact that by their very nature inflationary expectations apparently have a definite momentum and defy methods of any operational influence).

Following a number of clear failures of deflationary policy, the governments of most capitalist countries had to renege on their erstwhile assurances that they would "make short shrift" of inflation. Their economic experts now envisage very high rates of inflation in the period ahead as compared with the old standards.

Thus, in the early 1970s, there were repeated official assurances in the United States that the extensive anti-inflation programmes would reduce the CPI growth to 2.5-3 per cent a year, but developments in the subsequent period made such promises unrealistic. One analyst of hyperinflation declared:

> "Recent experience hardly gives much ground for believing that policy can be more successful in preventing inflation in the future."[1]

By the end of the 1970s, even the boldest anti-inflation forecasts no longer suggested that the CPI growth could be kept below 5-6 per cent.

The futility of all the attempts to stem the inflationary growth of prices shows once again that the roots of this process lie deep in the structure of the capitalist economy, and are built into its general mechanism.

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[1] Phillip Cagan, *The Hydra-Headed Monster. The Problem of Inflation in the United States*, American Enterprise Institute for Public Policy Research, Washington, 1974, p. 59.

CHAPTER FIVE

THE CRISIS OF NEOLIBERALISM AND THE EVOLUTION OF THE "SOCIAL MARKET ECONOMY" THEORY

The preceding chapters analysed Western concepts of the basic problems of capitalist reproduction, chiefly on the basis of Anglo-American economic writings, which continue to exert the crucial influence on the shaping of bourgeois economics as a whole and in the individual countries.

This chapter deals with the problems of reproduction as considered in bourgeois economics in the Federal Republic of Germany, whose historical conditions have left a specific imprint on its development. For a long time its economics was dominated by the neoliberal school, the German version of the neoclassical trend with its apologetics of free competition and the market economy. Only in the second half of the 1960s was there a growth of Keynesianism, whose official doctrine in West Germany has come to be known as the concept of "enlightened market economy".

1. Neoliberalism, Mouthpiece of Monopoly Capital Interests

Neoliberalism emerged in Germany in the late 1920s and early 1930s. One has to note the fact that the neoliberal doctrine began to develop in a country with embryonic liberal traditions, where the analysis of the market mechanism had never been of much importance, and where economic theories were dominated by ideas extolling the role of the state. By the mid-1930s, the ideologists of neoliberalism had formulated a kind of "neoliberal credo" which was most fully expressed in a special series of publications entitled "Economic Order" issued in 1937 by Walter Eucken, Franz Böhm and Hans Grossmann-Doerth.

The nazi takeover in Germany did not favour the use of neoliberal concepts in economic policy. Let us recall that the nazi leadership ignored economic theory as a whole and preferred economic concepts emphasising the constant and growing economic role of the state-bureaucratic machine.

After the Second World War, neoliberalism was given scope for development in West Germany. The rout of fascism signified not only the military, but also the political and economic defeat of German imperialism. Broad masses of German working people demanded an end to the hated past and the rule of the monopolists and Junkers, voicing their will for peace and the building of a new life. This urge was embodied in the formation of the German Democratic Republic, the first workers' and peasants' socialist state on German soil where the economic and political power of big capital was abolished once and for all. In West Germany, the country's future was a matter of an acute debate.[1]

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[1] A leader of neoliberalism and future West German Chancellor Ludwig Erhard said the following in an article entitled "Free Economy and Planned Economy": "In the debate on the Länder constitutions, the discussion of the future economic system quite expectedly unfolded on a wide scale... Apparently irreconcilable emotions flared up: some advocated a free economy, others a planned economy, some socialism, others capitalism" (Ludwig Erhard, *Deutsche Wirtschaftspolitik*, ECON, Düsseldorf-Wien, KNAPP, Frankfort on the Main, 1962, p. 19.)

The ruling circles and ideologists of imperialism, who increasingly resorted to Keynesian recipes, believed that West Germany was more prepared than any other country to adopt the Keynesian way of development. Here, government intervention in the economy had a long history, and for a lengthy period the extent of such intervention was even greater than it was in other industrialised countries, especially during the fascist period. German monopoly capital, the mainstay of fascism's domestic and foreign policy, which was responsible for the fascist crimes and for the nationwide crisis, and which had lost credence with the German working people, was in need of subtle methods for ideologically brainwashing the masses. On the territory occupied by US, British and French troops, the German bourgeoisie was looking for a flexible economic theory that would be anti-monopolist in words, and anti-democratic in deed, and that would, while being based on the conventional "respectable" politico-economic postulates, be sufficiently effective to cover up and keep the foundations of capitalism intact.

These requirements appeared to be most fully met by the neoliberal "social market economy" doctrine, which was designed to help the ruling class to navigate safely between the Scylla of an unregulated economy (19th-century and early 20th-century capitalism) and the Charybdis of public property. In the new doctrine, however, the main accent was on the stability of private property and the advantages of the free play of market forces over the artificially built-in systems of direct and indirect regulation of the economy, which were assigned only a corrective function. This warrants the classification of the initial version of the "social market economy" theory as a neoliberal trend in bourgeois economics.

The neoliberals dissociated themselves from the "historical school of classical liberalism" and set their face against Keynesianism, so putting in a claim for "originality" and "universality".

They believed that the historical approach was dangerous for science, because it destroyed faith in the natural system of law and economics. Böhm wrote that in the German historical school "science lost its Archimedian fulcrum to grasp the reality".[1] Having discarded the historical approach, the neoliberals advanced a "pure theory" or, as they put it, a "fundamental thinking" which was essentially a metaphysical method of analysis. While the "historical school" of German bourgeois political economy studied the concrete facts in their chronological and logical sequence (for they were to some extent influenced by Hegel's dialectics), the neoliberals operated with facts round their non-historical and immutable "ideal types" of the economy.

The neoliberals asserted that history has had, and will always have only two "ideal types" of the economy: "a free market economy", where individual economic units are linked through the market, and a "centrally planned economy", where individual enterprises are subordinate to a single governing centre. Under the first head, the author of this theory, Eucken, classified the economy of the free-competition period in the epoch of pre-monopoly capitalism, and under the second, the "central-command economy", including in it, on a par with each other, the planned economy of the USSR, the militarised economy of nazi Germany, the economies of the ancient Pharaohs, and even the 15th-century state of the Incas.[1] His idea was that social development should not be seen as a law-governed and historically rooted succession of formations, but in the light of the techniques used to

[1] Quoted in: Robert Naumann, *Theorie und Praxis des Neoliberalismus*, Verlag Die Wirtschaft, Berlin, 1957, p. 150.

[2] Walter Eucken, *Die Grundsätze der Wirtschaftspolitik*, Tübingen, 1952, pp. 58-61.

administer the economic process. Both these "types" have existed and still exist, according to Eucken, only as an ideal, for no more than approximate combinations of these will be found in actual life.

With the first successful steps being taken in building a socialist society in the other part of Germany, through the efforts of broad masses of people, the neoliberals thought it unwise to stand up openly in defence of capitalism, and so they posed this "cunning" question: "Isn't there a third way apart from capitalism with its concentration of power in the hands of the monopolists ... and the centrally administered economy?"[1] They sought to prove that there was a third way, and that it was the "social market economy". Erhard, for instance, asserted that such an economy was "a politico-economic system alongside the two existing ones".[2]

Let us recall that back in the 1920s, after the Great October Socialist Revolution, efforts to find a "third way" were made by Max Weber. This means that the neoliberals are not blazing a trail in this field. Eucken says that "capitalism" is a concept that cannot characterise the Western economy today and, for that reason, cannot provide a basis for theoretical studies.[3] Röpke simply proposed that "capitalism" should be replaced by some other "neutral and unsullied concept".[4] The Adenauer government asked Röpke to provide "scientific" evidence that the term "social market economy" was applicable to the economy of the Federal Republic of Germany. The term itself was introduced by A. Müller-Armack in the first postwar volume of

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[1] E. Preiser, "Walter Eucken in Memoriam". In: *Jahrbücher für Nationalökonomie und Statistik*, Vol. 162, Book 4, Stuttgart, 1950, p. 243.

[2] *Presskorrespondenz der CDU*, February 10, 1954.

[3] Walter Eucken, *Die Grundsätze der Wirtschaftspolitik*, pp. 58-61; also his *Die Grundlagen der Nationalökonomie*, Springer-Verlag, Berlin, 1950, pp. 60/61, 68, 80.

[4] W. Röpke, *Civitas Humana. Grundfragen der Gesellschafts- und Wirtschaftsreform*, Erlenbach-Zurich, 1946, p. 36.

the ORDO yearbook.[1] In 1950s, Röpke issued a book entitled *Is German Economic Policy Correct*?[2], with a preface by Adenauer, who said that "the new German economic policy can by right be called a 'social market economy'". Since then all government statements and CDU programmes have contained assurances of loyalty to the "social market economy".

Let us emphasise that its theorists had a definite political goal, namely, to denigrade the socialist planned economy, as will be seen, for instance, from a 1953 speech by Alexander Rüstow, which was published under the title "The Social Market Economy as a Counter-Programme against Communism and Bolshevism?" He said:

> "I am convinced that the most serious and worst weakness of our position is that to this very day we do not yet have a counter-programme against Bolshevism. That is why no task is more important or urgent for us than to create and work out such a programme."

At the same time, he admitted that it was futile to counter socialism with a patently pro-capitalist programme. He went on:

> "It is well known that Bolshevism has its own programme, and from the monolythic and consummate ideology of this programme it derives most of the strike force threatening us. If we turn to the entrepreneurs, i.e. to that stratum in whose hands the administration of the economy is mainly concentrated in all the free democratic countries, and if we pose this question: 'What kind of programme do our economic leaders present?', we

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1 *ORDO*, Vol. 1, 1948, p. 125 ff.

2 W. Röpke, *Ist die deutsche Wirtschaftspolitik richtig? Analyse und Kritik*, W. Kohlhammer Verlag, Stuttgart and Köln, 1950.

shall receive a truly staggering answer: 'None'."[1]

Rüstow goes on to assert that neoliberalism is the only "consistent and well-considered" programme for capitalism.

Social demagogy is of equal importance in that programme. Why is such an emphasis laid on the word "social"? Is there, after all, an economy in any society that is not social?

It turns out that "social" implies the bourgeois interpretation of the concepts of "freedom", "justice", and "affluence for all".

In Volume 22 of ORDO, published in 1971, the neoliberal Hans Lenel wrote that this doctrine formulates not only economic (as did the liberals of the past), but also socio-political goals.[2] He admitted that in the past the operation of the market economy had produced grave social consequences, drawing harsh criticism. To the question: "Do we have a social market economy?", Lenel replied that up until then there had been no such economy in agrarian, transport and social policy, and in industry "its principles have been practised with obstacles though consistently".[3] Let us note that Lenel's is not too encouraging an assessment for an advocate of the doctrine. While recognising the failures of the "social market economy", Lenel supports another formulation put forward by Karl Schiller in 1966, namely, "enlightened market economy", in the hope that the "enlightened" would salvage the market economy doctrine. Having analysed its principles, Lenel reached the conclusion that it did not signify a total departure from the "social market economy", but added that "at any rate, we have been moving away from it".[4]

[1] *Wirtschaft ohne Wunder*, Eugen Rentsch Verlag, Erlenbach-Zurich, 1953, p. 99.

[2] *ORDO*, Vol. 22, Düsseldorf, 1971, p. 31.

[3] *Ibid.*, p. 33.

[4] *Ibid.*, p. 44.

Erhard came out with an even more categorical statement. In a newspaper interview he expressed the apprehension that the "social market economy" was possibly coming to an end.[1]

This is a highly significant admission: the advocates of the "social market economy" doctrine have continued to support it as hard as they can, but are forced to recognise that it has been losing influence and popularity. Of course, they refuse to admit that ever broader strata of the working people reject the doctrine because they have realised that it expresses and safeguards the interests of big West German corporations. No wonder the "social market economy" is the basic doctrine of the CDU/CSU, the party of monopoly capital, and that big businessmen have stood up for it.

2. The Neoliberal Model of the Market Economy

The "social market economy" model is based on a number of principles which were most fully formulated by Eucken, who emphasises the following: free price formation and stability of money supply, competition without monopoly and stability of private property, economic independence and responsibility of business, and a limited economic role for the state.[2]

Although in the above list Eucken did not rank the *principle of private property* first, it is without doubt the basic one, and constitutes the substance of the doctrine. What bourgeois economists fear most is socialisation of the means of production, which is why they have been attacking the socialist planned economy and the property of the whole people. Without private property, they claim,

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[1] *Bild-Zeitung*, July 7, 1972.

[2] Walter Eucken, *Die Grundsätze der Wirtschaftspolitik*, pp. 254-289.

there can be no competition, no free price formation, and no independence or economic responsibility of business, i.e. without private property the "social market economy" model is inconceivable.

Eucken wrote:

> "The fundamental mistake in the economico-political discussions of the 19th and early 20th centuries was that the solution of sociopolitical problems was connected with the nature of property."[1]

Elsewhere, he asserted that

> "the solution of social questions should not be sought in the abolition of private property".[2]

This reveals the true purpose of the theorists of neoliberalism in the Federal Republic of Germany which is to preserve intact private property in the means of production, to safeguard the capitalist system, and to spread the idea of "individual freedom". When a neoliberal speaks about the individual and his freedom, he always has in mind individual capital, and not the factory or office worker, for his standpoint is that of the employer. This was very clearly expressed by the owner of an enterprise, someone called R. Valentin, in a speech at a CDU economic congress, when he declared to the applause of the hall: "The market economy is inconceivable without the entrepreneur with all his defects."[3]

It is quite clear that defence of the principles of private property meets the interests of those who own it.

Competition without monopoly is another constituent principle of the "social market economy" model. Eucken wrote:

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[1] Walter Eucken, *op. cit.* p. 270.
[2] *ORDO*, Vol. 2, 1949, pp. 46-47.
[3] *Wirtschaftstag der CDU, 1971*, Bonn, 1971, p. 62.

"Private property in the means of production is the premise for competition, just as competition is the premise for private property in the means of production not leading to disruptions in the social and economic spheres. Private property in the means of production requires control through competition."[1]

The neoliberals regard competition as the best and most perfect form of market relations. They also recognise four other market forms: partial oligopoly, oligopoly, partial monopoly and monopoly.[2] Under competition, the number of producers and their activities are not limited, but under partial oligopoly and oligopoly, they are. By partial monopoly they mean the domination of the market by one commodity producer, alongside of whom there are others whose activity is determined by the monopolist. Under monopoly there is only one commodity producer on the market. It turns out, therefore, that the market economy is characterised by one of these five forms.

For the neoliberals, whose concepts are based on everlasting and nonhistorical "ideal types" of economy, market forms (like the "centrally administered" economic forms) are not determined by the objective laws of economic development, and may be represented in any order in the various social formations. And because it is extremely rare for one commodity producer to operate on the market, the emergence of monopolies is regarded as an exception from the rule. With that kind of approach, there can be no question of a monopoly stage in the development of capitalism, whatever the actual facts suggest.

Muthesius does not see any monopolies at all,[3] while Böhm recognises the existence of monopolies

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[1] Walter Eucken, *op. cit.*, p. 275.

[2] Cited from: Robert Naumann, *op. cit.*, p. 193.

[3] Volkmar Muthesius, *Das Gespenst der Wirtschaftlichen Macht*, Fritz Knapp Verlag, Frankfort on the Main, 1960, p. 9.

only as "an imperfection in this world".[1] Lutz explains the emergence of monopoly and oligopoly by the fact that "the ideal of the competition order cannot be fully realised".[2] Rüstow held that monopolies could arise only in some spheres (transport and arms manufacture), and proposed that they should be nationalised.[3] But the view of most neoliberals was expressed by Eucken, who held that monopolies destroy competition and so contradict the substance of private property.[4] At the same time, Eucken opposed the nationalisation of monopolies or their control by the working people. He proposed that control should be exercised by a government agency.[5]

In these theoretical constructs the monopolies are not organically linked with the development of the productive forces and relations of production, but merely appear as a market category. They are regarded as a phenomenon clashing with the principles of the market economy model, the "ideal regulator of production", and so can allegedly be eliminated through state intervention. But a closer look at the "social market economy" doctrine suggests that by monopoly it does not so much mean private monopoly associations, as state property and planned administration of the economy. No wonder Böhm, a leading spokesman for the doctrine, wrote:

> "Under the circumstances prevailing today and expected to prevail in the future, the

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[1] F. Böhm, A. Rüstow, *Wir fordern von Regierung und Bundestag die Vollendung der sozialen Marktwirtschaft*, 1954, p. 40.

[2] *ORDO*, Vol. 5, 1949, p. 258.

[3] *ORDO*, Vol. 2, 1949, p. 134.

[4] Walter Eucken, *Nationalökonomie wozu?* Godesberg, 1947, p. 80.

[5] Walter Eucken, *op. cit.*, p. 294.

> private monopolist is the most harmless of all the monopolists."[1]

The neoliberals regard monopoly as the opposite of competition, and the two as mutually exclusive. But competition without monopoly is long since a thing of the past. Competition without monopoly under state-monopoly capitalism is like a forest without trees.

Competition without monopoly, like other postulates of this model, ignores the contradictions of capitalism and the incontrovertible truth that the whole process of monopolisation is determined by these contradictions, and intensifies and sharpens them. Absolute and relative concentration of production and capital extends the framework of private capitalist property, but does not transcend it, so that monopolisation cannot resolve the basic contradiction of capitalism between the social character of production and the private capitalist form of appropriation.

Free price formation is an important principle of the market economy model. While it may look like the similar principle of classical liberalism, it has, in fact, a number of fairly essential distinctions. First, the neoliberals require that this principle should be legislatively entrenched and maintained. Second, whereas the liberals of the past deduced from this principle only the "self-regulation" of capitalism, the neoliberals link it with economic growth rate, correct national economic proportions, and "fair" distribution, and indeed, imply a measure of government intervention in various spheres of economic life.

With the neoliberals, this principle is designed to have a coordinating function. Röpke wrote:

> "The substance of the market economy is that it replaces regulation of the economic

[1] Franz Böhm, *Die Aufgaben der freien Marktwirtschaft*, Isar Verlag, Munich, 1951, p. 60.

process by plan and orders of the authorities with regulation through the mechanism of free prices."[1]

The neoliberals claim that the "social market economy" best meets the interests of consumers, but, first, they say nothing about the fact that capitalist production is only ultimately connected with personal consumption and that capitalism has a sizable internal market of producer goods, arms and luxuries. Second, they confuse the concepts of "requirements" and "effective demand". The fact is that what operates on the market is not the requirements of the population but effective demand. In its drive to maximise profits, monopoly capital limits the working people's consumer demand, so objectively sharpening the contradiction between production and consumption. Consequently, what the "social market economy" doctrine in effect presupposes is not satisfaction of the working people's requirements, but the drive for profit.

The neoliberals' assertions that prices are an automatic regulator of capitalist production do not hold true either. They confuse the form and the substance of the phenomenon, and ignore the actual regulator of capitalist production, which is the law of value, a law that under capitalism spontaneously operates as economic regulator through the market price mechanism.

Being confronted in practice with constant breaches of "freedom" of price formation, the advocates of the "social market economy" cannot ignore this fact and so propose government intervention to restore this "freedom" and equilibrium in the economy. Actually, this principle has been repeatedly undermined by the government itself through its subsidies to private capital, which put the latter in a special position on the market and also through

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[1] Wilhelm Röpke, *Ist die deutsche Wirtschaftspolitik richtig? Analyse und Kritik*, p. 20.

the fixing of prices in industries with inadequate concentration and centralisation (like agriculture). The theory, however, provides for no real measures to combat the monopolies, the real culprits, who fix the highest possible prices for their products and so violate the principle of free price formation.

Stable money supply is the next constituent principle, and the neoliberals believe that it can quite be realised through monetary and credit policy. They pin great hopes on monetary and credit instruments in keeping the money supply stable, and believe that this creates conditions for the normal operation of competition, price formation, and economic equilibrium, and consequently, eliminates cyclical crises.

While being aware of the importance of the sphere of circulation, the neoliberals have not moved any closer to discovering its inner uniformities, and claim that crises can be averted through a manipulation of monetary and credit instruments, whereas these are, in fact, determined by the immanent laws of capitalist production and spring from the contradictions of the capitalist economic system. The neoliberals think that in the past economic crises were caused only by incorrect monetary and credit policies. Röpke wrote:

> "There is every evidence that their main causes ... lie in the imperfection of the monetary and credit system and the distribution of capital."[1]

Eucken hoped to create "monetary stability" by means of which market fluctuations could be eliminated.[2]

In their efforts to explain economic crises by disruptions in the monetary and credit sphere,

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[1] Wilhelm Röpke, *Die Gesellschaftskrisis der Gegenwart*, Eugen Rentsch Verlag, Erlenbach-Zurich, 1942, p. 196.

[2] Walter Eucken, *op. cit.*, p. 258. These ideas are now being developed by Milton Friedman.

the neoliberals, on the one hand, confused cause and effect, and on the other, asserted that economic crises were not connected with the mode of production and could occur in any social system. Böhm, for instance, held that under socialism crises should be even deeper than they were under capitalism.[1]

However, the facts show that the socialist system has never had any economic crises, that its economy enjoys constant and steady growth, while capitalism cannot escape economic crises because of its organic defects.

In an article entitled "The Social Market Economy Has Made Us Rich", Erhard wrote that "the worst economy is an inflationary one".[2] The neoliberals oppose inflation and sharply criticise the Keynesians for their theory of deficit financing, and also for their calls for "full employment", which allegedly undermines the stability of the currency. In the 1950s and the first half of the 1960s, when the neoliberal concept was applied in practice and its advocates held the key posts in the ministries and the central bank, monetary, credit and financial policy was aimed to stabilise money supply, balance the state budget, and set right the balance of payments. In that period, the Federal Republic of Germany secured a currency that was the most stable of all the other capitalist currencies, a surplus on its balance of payments, and growing gold and foreign exchange reserves. But the West German economy could not escape the growth of contradictions in the reproduction of capital, lower rates of economic growth, and partial crises in 1952-53, 1958 and 1963, and finally, the cyclical economic crisis of general overproduction in 1966-63.

The stable money-supply principle of the "social market economy" model is untenable because it is based on a false view of the substance of inflationary

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[1] Franz Böhm, *Die Aufgaben der freien Marktwirtschaft*, Isar Verlag, Munich, pp. 31-32.

[2] *Die Welt*, January 3, 1972, p. 6.

processes and the consequent ineffective methods designed to stabilise money supply and prices.

The neoliberals hold that gold and foreign exchange reserves are the best means of keeping the money supply stable. That is why they support measures aimed at building up the greatest possible surplus on the balance of payments. The record shows that they start from old notions dating from the period of metallic circulation, being unaware of the fact that in the absence of a gold standard, gold and foreign-exchange reserves lose some of their properties and require others. Just now these reserves, far from ensuring the stability of internal money supply, in effect are a source of so-called imported inflation. Had Eucken lived until 1974-76, he would have been amazed to see the West German gold and foreign-exchange reserves amount to the tremendous total of 80-90 billion marks and the country going through its worst bout of inflation since the Second World War.[1]

The *economic independence and responsibility of employers* is another important principle of the "social market economy" model, for it deals with the rights and duties of private entrepreneurs. Their rights were already envisaged in the preceding principles of the doctrine (namely, the stability of private property, free participation in competition and elimination of rivals, free pricing for their products, and wage restrictions). The neoliberals' view of employers' "economic independence" was well formulated by a mouthpiece of West German business circles, *Frankfurter Allgemeine Zeitung*. Considering Max Grundig and his realm, with a turnover of 1.5 billion marks, and a work force of 26,000, it wrote:

> "Here a monarch reigns. Although he is not an absolute sovereign, he is one of those who

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[1] *Monatsberichte der Deutschen Bundesbank*, May 1976, No. 5, p. 8*.

> knows how to make full use of the available opportunities... Max Grundig allows others to give him advice, but he takes the decisions himself, and quickly."[1]

This principle, like all the preceding ones, is designed to protect the interests of private enterprise, above all, of monopoly capital.

The role of the state is the last of these principles. Formulating the tasks of the state in the economic sphere, Eucken wrote:

> "The economic political activity of the state should be aimed at maintaining the existing forms of economic organisation, and not at directing the economic process."[2]

So the neoliberals abandoned the idea that the state should be neutral with respect to the economic process, but in contrast to the liberals, they hold that the market economy should not be left to shift for itself, because this leads to breaches of the "rules of the game" in competition. Observance of these "rules" calls for the intervention of a strong state. In contrast to the liberals who believed in the primacy of economics over politics, the neoliberals asserted the primacy of politics and the state over economics.[3] However, they confined the goals of state intervention to maintaining "a market economy that was capable of functioning",[4] so that the instruments used should not go beyond the "market" limits. In other words, the state is allowed to use only monetary and credit policy instruments.

The neoliberals also differ from the neo-Keynesians on the question of aims and methods of government economic policy, for the latter emphasise

[1] *Frankfurter Allgemeine Zeitung*, March 25, 1972, p. 17.
[2] Walter Eucken, *op. cit.*, p. 336.
[3] Quoted from: Robert Naumann, *op. cit.*, p. 154.
[4] A. Müller-Armack, *Wirtschaftslenkung und Marktwirtschaft*, Verlag für Wirtschaft und Sozialpolitik, Hamburg, 1947, p. 89.

state investments to compensate for inadequate private demand, and Eucken insisted that "the state is incapable ... of investing correctly and proportionately".[1] The neoliberals believe that the role of the state should be reduced to the functions of a soccer referee.

They are prepared to give up some of their principles so as to preserve the "social market economy" and to keep out any "planning principles". The prognostication and programming already used in other capitalist countries are regarded as unacceptable for the Federal Republic of Germany, and the very notion of "planning" is taboo. They will not even discuss the question of indicative planning. The goal set officially before the state in 1966 by the "big coalition", namely, to promote economic growth is still regarded by the CDU/CSU bloc as a concession to and a compromise with the Social Democrats, then in the government for the first time after the Second World War.

Consequently, the neoliberals' "ideal" model of the "social market economy" is free price formation on the basis of supply and demand of independent private proprietors in the conditions of competition protected by the capitalist state.

This model was on the whole applied in the West German economy from the period of postwar rehabilitation to the 1966-67 cyclical crisis of general overproduction. That period was marked by a mainly extensive type of economic development, i.e. a growth in the mass of exploited labour and investments entailing the creation of additional jobs. With a switch from extensive to intensive development, the growth of production is increasingly determined by a growth of labour productivity, instead of a growth in the mass of labour, and this is achieved above all through a renewal, expansion, and modernisation of the material and

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[1] Walter Eucken, *op. cit.*, p. 286.

technical facilities and broad application of scientific and technical achievements. Intensive economic development is closely bound up with the growth of production efficiency, which means a reduction in the per unit financial and material inputs. This calls not just for investment, but investment in industries which require especially large outlays on research and development, and which are for that reason less profitable, and investments in the infrastructure, education, science, and the services. Private capital is unwilling to move into these industries, and so the task is assigned by monopoly capital to the state.

However, the principles of the neoliberal model of the "social market economy" contained no provision for such state investment activity, because vigorous state intervention in investment activity clashes with the neoliberal doctrine.

Under the neoliberal economic policy, structural changes in the Federal Republic in the 1950s and 1960s were mainly characterised by a growth of industry's share in the GNP, while that of the "tertiary sector", which includes transport, communications, trade, education, public health, social needs, and science tended to shrink along with that of agriculture.

Thus, one of the defects of neoliberal economic policy is that it delayed the structural remodelling of the West German economy, and failed to create the conditions for the favourable use of scientific and technical progress. As a result, there was an underestimation and failure to stimulate the development of spheres like education, public health, culture, science, and the social infrastructure, and this largely explained West Germany's "technological gap", mainly with respect to the United States and also other developed capitalist countries: West Germany began to fall back in the competitive struggle and lose its positions in the world capitalist system.

3. Neo-Keynesianism and the "Enlightened Market Economy" Model

In the 1960s, some old principles of the "social market economy" model were modernised and new ones added, among them the policy of "commensurate growth" and "global regulation" of the economy. But this was not done by the neoliberals, but by the neo-Keynesians.

What was the reason for these changes? What made West German economists and statesmen tackle the problems of growth and indicative planning? There were at least three reasons: the economic competition between the two socio-political systems and the sharpening of inter-imperialist contradictions; the crisis of state policy based on the neoliberal doctrine; the objective course of economic development and the sharpening of the internal contradictions of capitalism.

Let us recall that immediately after the Second World War and up until the end of the 1950s, West Germany had a number of especially favourable conditions for monopoly capital. The Western powers, the United States in the first place, had put their stake on a revival of monopoly capital in West Germany and had virtually waived reparations so as to maintain the West German monopolies' production potential. What is more, there was an influx of foreign capital into West Germany, similar to that after the First World War. As early as the beginning of the 1950s, it was able to emerge on the world market. One should also bear in mind that the western part of pre-war Germany had always been its most industrialised area.

But, in spite of all these favourable factors, by the end of the 1950s the historical successes in socialist construction and the advantages of the planned economy in the German Democratic Republic were beginning to tell, as the first workers' and peasants' state on German soil switched its economic growth into high gear and began to reduce the economic gap between it and the Federal Republic of Germany. By contrast, from the end of the 1950s the latter's growth rate was slowing down.

This forced the West German capitalists to give serious thought to the prospects for economic growth and competition between the two systems. There were also the sharpening inter-imperialist contradictions and a fear of worsening their positions within the world capitalist system.

West German economists blamed the Federal Republic's slowing growth rate on the crisis of government economic policy oriented upon the neoliberal concept. Although in the 1950s, the Federal Republic had a relatively stable money supply, a balanced state budget, and a surplus on the balance of payments, one structural crisis followed upon another, until a cyclical crisis of general overproduction broke out in the mid-1960s. West Germany was faced with the need to change its economic policy. It became clear even to bourgeois leaders that if economic growth rates were to be stabilised there was a need to change structural and regional policy and to expand the scale and change the character and direction of investments into the infrastructure.

That was when the need was mooted in the Federal Republic for a more even distribution of the productive forces across the country, and of vertical and horisontal financial alignment of the Federation, the Länder and the municipalities. It was suggested that the infrastructure should be built up not only round the industrial agglomerations. The environmental problem was also a looming one, and plans were proposed for deconcentrating industry and manpower.

It became clear in the 1960s that sustained growth in the Federal Republic could be achieved only through a growth of labour productivity, which until then had entailed a growing capital intensity, and this signified a decline in the efficiency of production. This induced an analysis of the factors of economic growth, specially of the "third factor", i.e. the factor of scientific and technical progress. The question was how best to use it for growth and greater efficiency of production.

In these conditions, the neoliberal model of the "social market economy" began to backfire, neoliberalism was plunged into crisis, and neo-Keynesians came to the fore with their emphasis on the problems of economic growth.

The penetration of Keynesianism and the emergence of neo-Keynesianism in the Federal Republic of Germany proceeded in three stages: until the mid-1950s, from the mid-1950s to the mid-1960s, and from the second half of the 1960s. The first period was marked only by a "debate on Keynes", while the second saw the establishment of Keynesianism as a line of bourgeois economics in the country.

With the installation of the "big coalition" in late 1966, neo-Keynesian doctrine began to be practised in government economic policy. Here, the Social Democrats played an important role.

However, neoliberalism did not simply give up its positions to neo-Keynesianism. Under Keynesian influence, the "social market economy" model underwent something like an overhaul in which its old principles were patched up and new "important" parts—"global regulation" and economic growth policy—were fitted in. The neoliberal static model gave way to a dynamic model, "social" was replaced by "enlightened" or "capable of functioning", but the gist of the doctrine—market economy—remained the same.

Let us note that in the neo-Keynesian "enlightened market economy" model only the principles relating to monetary and credit policy and the government's role in the economy were substantially modified.

The neoliberals objected—if only in word—to any intervention in the "freedom" of price formation either by the state or by the monopolies. In the new model, monopoly prices are regarded as "normal" and the state is allowed to intervene in the process of price formation: it exerts a direct influence on the process (fixing prices for the output of its enterprises, mainly in branches like electric power and transport) and indirectly (subsidies to some industries and agriculture). The state had pursued such a policy from the early 1950s, although it was not envisaged by neoliberal doctrine. In the new model, this is regarded as a natural course of action, not in conflict with the market economy.

While the neoliberals held that the monopolies upset the principle of competition, the neo-Keynesians say that far from hampering, they, in effect, promote competition. The new model makes no secret of the fact that it is not the "individual", but the concern that is the subject of competition. The advocates of the "enlightened market economy" openly want the concentration of production and capital to be promoted, in view of West German transition from extensive to intensive development, when the emphasis is on higher labour productivity for faster economic growth.

That is why in the situation in which the concerns constitute the basis of the monopoly economy it is odd to hear the neoliberals say that the stronger the concern the greater the threat to the market economy, and that the concerns are no better than the centralised planning state.

It is hard to say whether this contains more naiveté or political demagogy: after all, Hans Lenel contrasted the state and the monopolies under state-monopoly capitalism when the power of the state has already coalesced with that of the monopolies.

The neoliberals' monetary and credit policy boiled down to stabilising money supply and balancing the government budget. They saw inflation as the main evil that had to be combated.

The new model brought to the fore a policy of economic growth with the use of deficit financing of investments and indifference to stable money supply, despite the fact that in the preceding period the SPD-FDP government had declared the fight against inflation to be one of its main tasks. Indirect regulation of the market by means of monetary and credit policy instruments was supplemented with financial measures, for which purpose a broad array of instruments was provided and set in motion.

State intervention in the reproduction of the whole of social capital marks a new stage in the development of state-monopoly regulation in the Federal Republic of Germany.

4. Economic Doctrines and Inter-Party Struggles

Economic growth models are directly connected not only with a line in bourgeois economics and the practice of government regulation, but also with the inter-party struggles for power, and, like economic doctrines generally, are extensively used by the political parties for formulating their social programmes. In the capitalist countries where several bourgeois parties compete for entry into the "push-button room", there is clear evidence of the connection between their economic platforms and practical policy with definite trends in bourgeois economics.

In West Germany, the two major bourgeois parties—the CDU and the CSU—are, in effect, two wings of a single whole. While there may be differences between them, they officially have a common economic programme which is based on the neoliberal doctrine of "social market economy".

Meanwhile, the SPD, contesting the right to govern the country against the CDU/CSU bloc, has been departing from the "social market economy" concept and looking increasingly to neo-Keynesianism, another trend in bourgeois economics, and gradually borrowing some of its basic principles from it.

Since the SPD had openly switched to the neo-Keynesian version of bourgeois reformism long before its electoral victory in 1969, a sizable part of monopoly capital realised the emergence of an acceptable alternative to CDU/CSU policy. Monopoly capital also took into account the record of the Social-Democratic government in the Weimar republic, when right-wing Social-Democratic leaders adopted reformist ideas in theory and practice within the framework of capitalism.

Like the SPD, the Social-Democratic parties of other West European countries in their programmes and decisions either deny the class character of capitalist states or describe it as "fair" and "democratic". A resolution of the 14th Congress of the Italian Social-Democratic Party in 1966 described modern state-monopoly capitalism as a "fair and freely integrated society". We find similar assessments by the Social-Democratic parties of Sweden, Denmark, and Norway.

Social-Democratic theorists have long since rejected the idea that present-day capitalist society has a class nature. The West German Social-Democrats have borrowed the bourgeois slogans of "pluralist society" and "pluralist democracy", the latter implying an equal participation by parties, government, employers' unions, and trade unions in the making and implementing of decisions. This is an attempt to cover up the true nature of the economic and political power in the capitalist countries, determined by a coalescence of the power of monopolies and the state.

But the SPD leadership had to reckon with the mood of the masses and the rank-and-file membership. That is why from the end of the Second World War until the adoption of the Bad Godesberg programme in 1959, SPD congress decisions contained demands for important transformations of the existing social system. Thus, the 1946 Hannover Congress announced that socialisation of the means of production was one of the party's main demands. Party chairman Kurt Schumacher said at the time that socialism was on the order of the day. In a 1947 theoretical discussion most Social-Democratic economists did not question the need for socialising the means of production, and differed only on the ways of doing this.

But even then, right-wing Social-Democratic theorists asserted that Marxism was allegedly irrelevant in the new conditions. Accordingly, the SPD party press began to carry articles warning that if it departed from Marxism, the party could become an amorphous party of the "middle".[1] The Action Programme adopted by the 1954 Congress (in addition to the Dortmund Action Programme of 1952), still contained the demand for a socialisation of the means of production in the key heavy industries, but the accent was now increasingly on "public control".[2] The question of socialising the means of production was pushed into the background, behind a screen of dissertations about the differences between nationalisation and socialisation. Social-Democratic theorists attacked nationalisation, denied that it had anything to do with the process of

[1] It is noteworthy that at the SPD Congress held in Hannover in April 1973 it was Willy Brandt, among others, who said that that was what the party had in fact become.

[2] At the SPD Congress in 1973, this was the key task in the formulation of a long-term programme for the 1973-85 period.

socialisation, which they saw as the formation of group private property, and switched to the idea of state-monopoly regulation of economic development. The intervening period and the goals for which the SPD has been striving, as will be seen from the decisions of its last few congresses, show that it has failed to produce a theory of its own and has adopted bourgeois concepts so as to adapt state-monopoly capitalism to the changing situation through bourgeois-democratic reforms.

But when the SPD became the ruling party and its theoretical concepts were confronted with practical policy, a left wing within the party began to gather strength. It consists of old party members like J. Stefan, Karl Zinn, Werner Meissner, Rudi Arndt, and Erhard Eppler, and a large contingent of "young Socialists". But this left wing is not united either, and alongside the critics of the right-wing leadership there is a growing demand for adoption of the Marxist-Leninist theory and the need to build socialism. A month before the SPD Congress in April 1973, the "young Socialists" held a congress under this motto: "Socialism because it is wise". The draft long-term programme put before the SPD Congress was sharply criticised, chiefly because it did not contain any real analysis of the existing system, of economic power, and the class struggle, and any perspectives of socialism.

The Saarbrücken Congress of the SPD in 1970 decided to set up a commission headed by Helmut Schmidt to frame a long-term economic, social and political action programme. Its economic part was to consist of an indicative general plan with targets and guidelines for 12 years. In the summer of 1972, the commission circulated its draft economico-political guidelines for 1973-85 among the party organisations for debate.

The emphasis in the draft was on reforms in the country's economic and social life designed to bolster the market economy within whose framework there was to be "global regulation" with some elements of planning.

Thus, more important tasks of government regulation were brought to the fore. This will be seen from the fact that the share of the state in the gross national product is to go up from 27.9 per cent in 1970 to 34 per cent in 1985.[1] The state was to spend more for education, research, transport, and public health, covering the larger outlays through a number of tax reforms, in accordance with the decisions of the 1971 SPD Congress on fiscal policy designed to increase tax revenues and use them to expand the sphere of the social services and improve the "quality of life". Tax revenues were to be increased through the abolition of some of the privileges established in the period of rehabilitation, the introduction of additional taxes on output polluting the environment, and higher taxation rates on the growing price of land.

The draft admitted that "the property in the means of production in industry, trade, and the handicrafts is still in a relatively few hands".[2] Accordingly, there was a provision for extending participation by wage labour "in the co-ownership of capital", with special emphasis on the "socio-political importance of participation by the wage workers in the growth of the means of production".[3]

The Social-Democrats believe that by supporting the trade union demands for parity participation in supervisory councils they are depriving monopoly capital of management in industry and of the right to decide on economic policy. Here they echo the ideas of US bourgeois theorists of the "managerial revolution", among them James Burnham and Adolph Berle.[4]

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[1] *Langzeitprogramm 1*, Verlag Neue Gesellschaft, Bonn-Bad Godesberg, 1972, p. 32.

[2] *Ibid.*, p. 215.

[3] *Ibid.*

[4] For details see next chapters.

Of course, parity participation by trade unions n supervisory councils of enterprises is much , etter than the terms accepted by the bourgeois (DU/CSU parties, but even that does not give the trade unions equal opportunities with the private property owners in industrial management. At best they have only one representative on boards made up of businessmen and their representatives. With private property, those who own the controlling interest still decide the destiny of enterprises and their economic activity.

The draft also dealt with another element of the relations of production, namely, the distribution of incomes and property, and here we have a Social-Democratic version of the bourgeois theory of "income distribution". The policy of promoting savings and the working people's participation in the distribution of profits will not make their incomes equal to those of the financial tycoons even in a hundred years. The Social-Democratic reforms cannot bridge the income gap between labour and capital.

The long-term programme was harshly criticised both from the right, by the neoliberals siding with the CDU/CSU, and from the left, within the SPD, and was not adopted by the Hannover Congress in 1973. Another commission—a working group—was set up to formulate policy priorities, and a special institute to study the fundamental aspects of "democratic socialism". The party started a debate on theoretical issues. At the Hannover Congress, Schmidt admitted that the SPD had failed to put before the electorate an explicit theory of social development. In the course of a two-year debate, the original draft was modified, and a new version, published in February 1975, was adopted by the Mannheim Congress in the autumn of 1975. It is a long-term programme, for it formulates the party's goals and lines of activity until 1985. It says that the SPD continues to rely on the basic principles formulated in the Bad Godesberg programme of 1959. The new programme concentrates on various aspects of social development, and maps out guidelines and goals of SPD activity without giving any quantitative assessments or indicators.

An analysis of the new SPD programme leaves no doubt that it has not gone beyond bourgeois-reformist notions about the development of society, and has not provided a socialist alternative. It starts from incorrect assessments of the key issues in present-day economic, social and political life in the country. Its analysis of the social system underrates the importance of the concentration and monopolisation of power even as compared with the Bad Godesberg programme.

At the same time, the programme contains no provision for moving closer to the trade unions either in the economic or the socio-political spheres. It even clashes with the trade union programme demands for the nationalisation of the big concerns. The premise and content of Social-Democratic policy is the maintenance and stabilisation of the existing system of domination and subordination. It does not contain any anti-monopoly or anti-capitalist strategy, as distinct from the programmes of some other Social-Democratic parties. Its analysis of the world capitalist economy does not indicate the true causes of the crisis of the mid-1970s or the prospects for overcoming it in the future.

Here and elsewhere, the authors of the programme display their complete impotence, because they rely on bourgeois science, which has itself long been in a state of crisis.

CHAPTER SIX

THE CRISIS OF BOURGEOIS CONCEPTS OF INTERNATIONAL MONETARY RELATIONS AND BALANCE-OF-PAYMENTS REGULATION

The crisis of bourgeois theories of the world capitalist monetary and financial mechanism is an expression of the present stage in the crisis of bourgeois political economy. At the same time, the irrelevance of bourgeois concepts of international monetary relations is an important aspect of the deep-going structural crisis which in the mid-1960s hit the postwar Bretton Woods gold-exchange standard system.

Let us note that it is much harder to establish the connection between practice and theory, and between the restructuring of various parts of the mechanism of the capitalist economy and the general trends in its evolution in the sphere of international monetary and financial relations than it is in any other sector of the economy. Monetary policy is characteristically an inconsistent, halfway pragmatic and utilitarian policy. This is chiefly because any practical steps in restructuring the international monetary system involve acute struggles among the leading imperialist states, and also contradictions between industrialised and developing countries.

Present-day bourgeois concepts of international monetary relations took shape along the traditional lines of bourgeois economics—Keynesian and neoclassical (neoliberal). They now serve governments and international organisations in the capitalist world as a theoretical backup for numerous programmes designed to find a way out of the bog of the monetary crisis.

This chapter contains a critical analysis of the leading bourgeois theories of international monetary relations: both concepts of balance-of-payments regulation and theoretical notions concerning international liquidity. It also shows the close interconnection between these two aspects of the monetary problem facing capitalism.

1. Monetary Crises and the Evolution of Bourgeois Concepts

Capitalist economic relations of the free competition period were ideologically substantiated by classical bourgeois political economy and then by vulgar political economy in the 19th century, their main premise being that capitalist market relations ensure stable economic development ruling out general overproduction and chronic unemployment. In the 18th and 19th centuries, bourgeois economists asserted that the economic mechanism based on private capitalist property and the free play of market forces also helped to re-establish the disrupted equilibrium of international money flows mediating the external economic exchange of goods and services.

This concept had for its institutional basis the currency and monetary system of the gold standard, which corresponded to free-competition capitalism. Within its framework, final settlements on international balances of payment were effected by means of spontaneous flows of gold from one country to another along private channels. The theory of a self-correcting balance of payments was formulated by David Hume, John Stuart Mill and David Ricardo and was generally accepted in the 18th and 19th centuries.

The classical mechanism of the gold standard eventually became a drag on economic development in the capitalist world, and finally collapsed in the 1930s. It was replaced in internal money circulation by paper money which was not convertible into gold, while a gold-exchange standard was gradually established in monetary relations among states. That was the name given to the mechanism of monetary settlements based on the extensive use in world commerce of two key national currencies—the US dollar and the British pound sterling—as payment and reserve instruments on a par with gold.

The grave economic upheavals demonstrated the failure of the then dominant bourgeois theories, including the concept of a self-correcting external economic exchange, which, it will be recalled, led to the emergence of Keynesianism as the ideological and theoretical reflection in the bourgeois consciousness of the development of monopoly capitalism into state-monopoly capitalism.

The Keynesian concept of keeping external payments in equilibrium took shape in the 1930s and 1940s. Although it was a direct product of Keynes's "general theory of employment", it was set forth mainly by some of his followers, among them, Frank Paish, Joan Robinson, and Roy Harrod. A contribution to the theory was also made in the early 1940s by Gottfried Haberler, Walter Salant, Charles Kindleberger, Lloyd Metzler and Fritz Machlup.

Let us note that Keynes and his followers took an essentially different approach to the maintenance of internal and external economic equilibrium. Keynes's assumption was that equilibrium in the internal economy (i.e. the state of full employment) could not be achieved without government regulation of the reproduction process. As for the "external balance" (equilibrium in international payments), "the Keynesian revolution" did not, in effect, shake the idea that the latter could be automatically re-established by means of changes in internal economic conditions caused by the very same disruptions of the payments balance.

Keynes and his followers traditionally regarded the phenomena now referred to economic policy instruments (like interest rate) as variables whose values were automatically determined by the spontaneously shaping state of the balance of payments. The value of unknown quantities like employment, income, and the new balance of payments were established on the "output" side of this model. Consequently, it had a "forecasting" character and implied that the government was to pursue what could be called a "neutral economic policy".

The new approach to the problem of external equilibrium, which consisted in the latter being regarded as one of the economic goals of deliberate government policy, was first proposed in the early 1950s by the Englishman James Meade and the Dutchman Jan Tinbergen, who effected independently of each other an inversion of the traditional model. Their constructs optimised the values of employment, real income and balance of payments and, on the strength of these, the necessary values of the endogenic variables characterising the instruments of economic policy are calculated with the use of mathematical formalism. It is then up to the government agencies to determine the parameters of the goals and to "tune" the instruments accordingly.

It was Keynes who theoretically substantiated in the 1930s and 1940s the institutional transformation of the capitalist monetary mechanism. At the end of the Second World War, Keynes put forward a plan for the postwar reorganisation of the international monetary and financial system containing a proposal for an International Clearing Union.

Many of his more "radical" ideas (notably, the issue of an international currency not secured with gold deposits, and the automatic crediting of debtor-countries in the course of international settlements) were designed above all to ease Britain's monetary and financial condition. This, however, ran counter to the efforts of the US ruling circles to establish the dollar as the dominant currency, which is why they rejected the Keynes Plan.

Relying on its economic and financial superiority, the United States imposed its project on Britain and the other capitalist countries in the course of an international monetary conference held at Bretton Woods (USA) in 1944. The conference adopted an agreement setting up the International Monetary Fund (IMF) and establishing the main features of a new monetary mechanism which were above all in line with the interests of US imperialism.

But while rejecting some of the concrete propositions in the Keynes Plan, the US ruling circles used his conception of international liquidity representing paper and credit instruments instead of gold. The United States succeeded in having it adopted in a form that best promoted the external economic expansion of US imperialism and helped to impose the "dollar standard" on the other capitalist countries. The US leaders also adopted Keynes's idea of regulating monetary relations through a special body, the IMF. It enabled them to maintain some control over the monetary and financial policies of other capitalist countries and the kind of "order" they wanted in international monetary relations.

One has to recognise, therefore, that the shaping of the postwar gold exchange system was largely inspired by Keynes's ideas. At the same time, these were combined with elements of the "liberal", free trade external economic concept which then met the interests of the United States.

The subsequent evolution of the postwar capitalist monetary mechanism in the 1950s and 1960s also proceeded with the continued introduction of Keynesian principles. In this context, an English economist M. S. Mendelson summed up the development of the IMF, which was at the centre of the postwar capitalist monetary system, and wrote:

> "In the first quarter century, the Fund has moved very far from its constricted beginnings ... towards the more expansive institution envisaged by Keynes. He wanted an organisation with large resources, providing fairly ready access to credit, promoting stable but not rigid exchange rates, run by technicians rather than governments, and with power to issue its own international currency. Much of this has gradually come to pass."[1]

In the late 1960s and early 1970s, the workings of the internal contradictions of state-monopoly capitalism led in most industrialised capitalist countries to a rapid growth of inflation which ceased to be a factor stimulating economic growth and became a factor slowing it down and generating a trend towards economic recession. This plunged into crisis the state-monopoly regulation of economic relations in the individual countries and within the framework of the world capitalist system.

The system of monetary settlements which took shape after the Second World War was also deeply contradictory from the very outset. For its part, it stimulated inflation throughout the capitalist world and acted as a transmission mechanism

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[1] M. S. Mendelson, "Has the Fund Gone Keynesian After All?" In: *The Banker*, London, May 1971, p. 498.

spreading inflationary impulses from the United States to the other capitalist countries. The monetary disproportions and the upheavals on the world money markets began to have a disorganising effect on the economy of the capitalist countries, to deepen the social antagonisms and to worsen the structural crisis of the Bretton Woods monetary system. It became obvious that the attempt to set up a reliably governable "monetary stimulator" of the economic outlook on the basis of Keynesian ideas was not a success.

From this it followed that the Keynesian concept of international monetary and financial relations or, at any rate, the version of the concept which was translated into practice after the Second World War proved to be unsatisfactory. The neo-Keynesians themselves claimed that the monetary upheavals resulted from the failure fully to implement Keynes's ideas in the establishment of the postwar monetary system. They pointed, above all, to the fact that the role of international payments instruments had been assigned to the national currencies of individual countries susceptible to internal economic ills, instead of the collective currency that was to have been set up by means of international state regulation.

The creed of the present Keynesian trend is that the mechanism of monetary and credit ties should be further expanded and improved through the interstate centralisation of monetary reserves. The Keynesians wanted credit payments instruments to be made explicitly international, with a restriction on the regulating functions of gold and a further reduction of its use in international commerce.

As the crisis of the dollar deepened, the centre stimulating Keynesian experiments in the monetary sphere increasingly moved to the United States, with Robert Triffin regarded as the most consistent advocate of the international money concept. In Britain, the Keynesian tradition in international liquidity has been continued by Alan Day, Maxwell Stamp, Roy Harrod, and James Angell, among others. In France, many elements of this concept will be found in the works of dirigists like F. Perroux and Jean Denizet.

Following the failure of Keynesian economic policy in monetary and financial relations, there was a strengthening of the neoclassical (neoliberal) trend in this sphere of bourgeois economics as well.

Neoclassics, with their traditional metallic theory of money, which identified the latter with precious metals, say that the monetary crisis was chiefly caused by the abandonment of international settlements in gold and the extensive use of the dollar and the pound sterling as international reserve and payments instruments. Their "constructive" concepts are based on defence of gold monometallism (which in the capitalist world was finally destroyed by the economic crisis of 1929-33) and the establishment of an international gold standard.

In our day, it is France and partially some other West European countries that have become the chief critics of Keynesianism from the standpoint of the metallic concept of money. They have been carrying on a struggle against the hegemony of the dollar in their efforts to secure an influence on world monetary affairs commensurate with the changing balance of strength in the international arena in their favour. This approach is most clearly expressed by the influential French economist Jacques Rueff. The "metallic" approach is also shared by some bourgeois economists in other countries, among them Michael Heilperin in the United States and Jan Shannon in Australia.

However, at the present stage the neoclassical approach to the problems in restructuring monetary and financial relations is characterised not so much by the "metallic" version as by orientation upon *freely fluctuating* ("floating") exchange rates under the impact of supply and demand.

At first, the idea of establishing floating exchange rates appeared to be purely academic and without any real chance of success in practice. However, the inadequate effectiveness of the national instruments of monetary and financial regulation and the exhaustion of the potentialities for further expansion of the international "buffer" monetary and credit superstructure, the growth of inflation and its increasingly uneven development in the individual countries, inducing the need for periodic adjustments of the official exchange rates, caused the idea of floating rates to be brought to the fore in the late 1960s and early 1970s. The US ruling circles seized upon it as a means of effecting the "market" devaluation of the dollar with respect to the currencies of the other countries that were the most dangerous trade rivals of the United States, above all the Federal Republic of Germany and Japan.

Apart from Friedman and Meade, this concept was and is accepted by many other well-known bourgeois economists, among them Haberler, Machlup and Houthakker in the United States, Scammell in Britain, Hirsch, Müller-Armach, Erhard in West Germany, Lutz in Switzerland, and Lundberg in Sweden.

Let us note that the crisis of the neoliberal and the neo-Keynesian concepts induced them to move somewhat closer to each other. This trend apparently springs from the vital need for a practical solution of the problem of monetary reform.

The ruling circles of the leading Western countries are feverishly seeking ways out of the crisis "troubles", and one of their lines is the attempt to adapt capitalism to the new conditions through the current restructuring of the monetary system.

In early 1976, at the fifth meeting of the IMF Interim Committee held in Kingston, Jamaica, an agreement was reached on a reform of the international monetary mechanism, described in the West as a "milestone" in the capitalist world's official switch from one international monetary system to another. However, the ongoing reform is limited and incomplete, and does not in any sense solve the urgent problem of effecting a radical reconstruction of the capitalist international monetary mechanism.

The Jamaica agreement is ultimately no more than a temporary and unstable compromise among its signatories, and it contains the embryo of new conflicts and divisions among the leading industrialised capitalist countries.

Nor is the agreement a "pure product" of any of the three bourgeois economic theories considered above in general terms. It could be described as a symbiosis of the neo-Keynesian and the neoclassical approaches, the former contributing the idea of demonetising gold, and the latter the "floating" exchange rates, so leaving neither side fully satisfied. It does not eliminate the contradictions between the schools and does not testify to the elaboration by bourgeois economics of a synthetic concept of monetary reform.

2. Balance-of-Payments Equilibrium as a Goal of Economic Policy

The spread of state-monopoly capitalism to international economic and, in particular, monetary and financial relations, has raised the question of the goals to be pursued by the government regulation of monetary relations and the tasks of monetary policy. Bourgeois economists believe that these amount to keeping a country's international balance of payments in equilibrium, a balance that under the gold standard was allegedly self-correcting because of the operation of the mechanism set in motion by the very disruptions of the equilibrium.

Thus, the US bourgeois economist Marina von Neumann Whitman writes:

> "We have come to recognise that the automatic 'classical' price-adjustment process may be inoperative in a Keynesian world of unemployment and downward rigidity of wages and prices. Moreover, we know that there are real economic costs involved in automatic adjustment via income changes... Acknowledging these facts, economists have come to regard 'external balance', that is, balance-of-payments equilibrium, as one of the specific economic objectives of deliberate governmental action, rather than as something that will take care of itself."[1]

Bourgeois economists also began to discuss the task of attaining balance-of-payments equilibrium within the overall system of the main goals of the capitalist state's economic policy, and the priority and hierarchy of these goals, which are regarded as the angles of a polygon.

The most elementary system is presented in the form of a triangle of economic goals. Thus, a report by the Economic Advisory Council in the Federal Ministry for Economic Affairs (FRG) in 1956 said that economic policy should have to pursue three goals: "to keep the purchasing power of the currency stable, to keep employment of the productive resources as high as possible, with equilibrium of the balance of payments on the basis of a free international exchange of goods and services." The Act on the Constitution of a Board of Experts for the Assessment of Overall Economic Trends says that it is to analyse

> "how stability of the price level, a high degree of employment and international eco-

[1] Marina von Neumann Whitman, *Policies for Internal and External Balance*, Princeton University, 1970, pp. 1-2.

nomic equilibrium can be maintained with constant and adequate economic growth in the framework of a free market economy."[1]

(Here we find a "square", i.e. the four main goals of economic policy.)

Bourgeois economists admit that these goals are mutually incompatible and constantly produce situations of conflict. The US economist Jacob Viner also emphasised the importance of these four goals as the main ones in economic policy and described these situations as follows:

"I do not claim that it is possible even in theory completely to harmonize all the legitimate economic objectives of government, or even to escape occasional fairly serious conflicts between objectives which can be resolved only by compromising or temporarily abandoning one or more of them."[2]

Under "normal" conditions, which are taken as the starting point, the bourgeois state gives priority to the attainment of internal economic objectives, but as experience shows, stepped-up economic growth, which also entails the securing of a high level of employment, has a tendency to disrupt a country's balance-of-payments equilibrium, so causing either a deficit or a surplus.

Sooner or later, a protracted deficit on the balance of payments forces the government of a capitalist country to take so-called deflationary measures, which mean cuts in government budget spending, a higher banking rate, and various acts to make it harder for employers and consumers to obtain credits. A direct outcome of these measures is a trend to falling investments

[1] Quoted from: A. E. Ott, "Magic Polygons in Economic Policy. A Theoretical Analysis of Conflicts of Economic Targets." In: *The German Economic Review*, Stuttgart, 1971, Vol. 9, No. 1, pp. 11-13.

[2] Jacob Viner, *Problems of Monetary Control*, Princeton University Press, Princeton, New Jersey, 1964, p. 6.

in both the private and the state sectors, a slowdown in the growth or a reduction in the volume of industrial output, and a slowdown in scientific and technical progress.

It looks as though such key goals of internal economic policy as stable economic growth and full employment cannot be attained at all.

A protracted surplus on the balance of payments inevitably forces that country's government to take steps to eliminate the excess foreign receipts, as compared with payments, by expanding imports and restricting exports. These measures ultimately boil down to stimulating internal effective demand and are, consequently, expansionist. But simultaneously they tend to increase inflation, and so clash with such a constant goal of economic policy as the maintenance of stable prices.

As a result, because of the contradictory nature of the goals of economic policy, the task of attaining each of these goals is in reality transformed for the capitalist state into a more complicated problem, or as Marina von Neumann Whitman put it, into "the problem of simultaneously achieving external and internal (full employment and price stability) balance".[1] Bourgeois economists seeking to obscure the acute contradictions of the capitalist economy for apologetic purposes claim that the incompatibility of the goals of economic policy is no more than "tentative".

But, as we shall show below, bourgeois economics has proved incapable of producing a concept that could claim to fulfil the tasks formulated above.

3. The Metallic Concept of World Money

The advocates of the metallic approach to international monetary relations are, in effect, trying

[1] Marina von Neumann Whitman, *Policies for Internal and External Balance*, p. 2.

to revive the traditional theory of a self-correcting balance of payments, a theory that dominated bourgeois political economy in the 18th and 19th centuries. It had three main sources: the view of the capitalist market economy as a system guaranteeing realisation of the total product and full use by society of the available production and manpower resources; the then prevailing metallic concept of money; and the quantity theory of money.

Given these premises, bourgeois economists held that the balance of payments tended to correct itself in the following way. When a balance-of-payments deficit develops, gold begins to flow out of the country. The reduction in the quantity of money in circulation and the consequent reduction in costs lead to a reduction in prices. This, for its part, begins to have a stimulating effect on exports from the country and a depressing effect on imports, and this is what brings the balance of payments back into equilibrium and reverses the flow of gold into the country. When a sizable surplus emerges on the balance of payments, developments run in reverse: influx of gold—more money in circulation—growth of prices—switch by money owners at home and abroad to purchasing goods made in other countries where they are cheaper—growth of imports which, alongside the reduction of exports, results in the elimination of the surplus and stops the influx of gold. In this context, Ricardo asserted that

> "metallic currency has its remedy in the import and export of precious metal, which immediately enters circulation as coin and thus, by its inflow or outflow, causes commodity prices to fall or rise".[1]

Thus, according to the theory, the operation of the self-correcting mechanism is confined to the

[1] Quoted from: Karl Marx, *Capital*, Vol. III, p. 548.

monetary sphere. Characterising this aspect of the theory, Metzler wrote:

> "The important feature of the classical mechanism ... is the central role which it attributes to the monetary system. The classical theory contains an explicit acceptance of the Quantity Theory of Money as well as an implied assumption that output and employment are unaffected by international monetary disturbances."[1]

Marx showed very well the scientific untenability of the concept of a self-correcting balance of payments and the underlying quantity theory of money. He wrote:

> "It is indeed an old humbug that changes in the existing quantity of gold in a particular country must raise or lower commodity-prices within this country by increasing or decreasing the quantity of the medium of circulation."[2]

Marx showed that in metallic monetary systems the level of commodity prices does not depend on the quantity of money in circulation but on the ratio between the value contained in a commodity unit and the value of the money unit. That is why the flow of gold from one country to another under the influence of changes in the balance of payments cannot automatically cause either a rise or a lowering in the level of commodity prices and, consequently, cannot correct the commodity flows in international trade.

Subsequently, with the broad spread of credit money and the development of the banking system, the self-correcting balance-of-payments concept was somewhat modified, with the introduction of the

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[1] Lloyd A. Metzler, *Collected Papers*, Harvard University Press, Cambridge, Massachusetts, 1973, p. 3.

[2] Karl Marx, *Capital*, Vol. III, p. 551.

analysis of the behaviour of a central-banking unit and consideration of the role of banking rate.

Bourgeois economists who are still strongly influenced by the traditions of "economic liberalism" describe the monetary system of gold monometallism mainly in idyllic tones. They claim that it prevented the emergence of inflation and other monetary disturbances, eased the crisis upheavals in the capitalist countries, and regulated international economic exchange and the payments turnover.

It was Marx who gave a truly scientific analysis of the role of gold in the mechanism of automatic influence of external economic exchange and the payments balances of the capitalist countries. According to Marx, the international movement of gold, "by virtue of the specific character of precious metal as capital in money-form",[1] exerts a definite influence on the interest rate, and the latter, for its part, may also influence commodity prices. Consequently, because of the participation of the credit system in the functioning of the capitalist economy, the inflow or outflow of gold can, in certain circumstances, cause a tendency of the balance of payments towards a state of equilibrium.

At the same time, Marx showed that the operation of economic forces stabilising the balance of payments, to which the authors of the self-correction concept referred, was secondary with respect to the processes in capitalist reproduction. Prices will respond to the export or import of gold only when the tendency caused by the movement of gold coincides with the influence exerted on prices by the current phase of the cycle. Being in contradiction with the flow of the economic conjuncture, the equilibrium forces are inexorably carried away by that flow. Describing the influence which

[1] Karl Marx, *Capital*, Vol. III, p. 571.

changes in the quantity of gold in a country as a result of its inflow or outflow had on commodity prices and general economic conditions, Marx said that the change in the quantity of gold acted

> "like a feather, which, when added to the weight on the scales, suffices to tip the oscillating balance definitely to one side; it acts because it arises under conditions when any addition decides in favour of one or the other side... Similarly, on the other hand, even a very considerable drain of gold is relatively ineffective if it does not occur in the critical period of industrial cycle."[1]

Criticising the bourgeois "metallic" theory of money, Marx emphasised the historical limitations of the gold standard:

> "The entire history of modern industry shows that metal would indeed be required only for the balancing of international commerce, whenever its equilibrium is momentarily disturbed, if only domestic production were organised. That the domestic market does not need any metal even now is shown by the suspension of cash payment of the so-called national banks, which resort to this expedient in all extreme cases as the sole relief."[2]

The theoretical arguments of bourgeois economists variously looking to the "metallic" tradition have been most fully set forth in the works of Jacques Rueff.[3] In his view, the "monetary sin" of the capitalist world consists in limiting and stopping the use of gold in international settlements, departure

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[1] *Ibid.*, pp. 571-572.

[2] *Ibid.*, p. 517.

[3] Jacques Rueff, *La Réforme du système monétaire international. Pour un succès immédiat et certain*, Paris, 1973; also his: *Le Péché monétaire de l'Occident*, Plon, Paris, 1971.

from the gold standard and its replacement by the gold-exchange standard, and later by the purely dollar standard. He says that this evolution of the monetary system had three main consequences for the world capitalist economy.

One of these is the maintenance over a long period of a balance-of-payments deficit by the reserve-currency countries, notably, the United States, a practice which up to a point did not cause much trouble. Rueff says this was due to the fact that under the gold-exchange standard the citizens of the countries whose currencies enjoy the status of international money (for all practical purposes, it is now only the United States) cover their external liabilities with national paper money, so that the dollars passing into the hands of foreigners, in effect, do not leave the channels of circulation. As a result, despite the balance-of-payments deficit, there is no automatic reduction in money supply in the United States or a corresponding reduction in aggregate purchasing power and a shrinking of the credit base, as it should have occurred under the gold standard. To the extent to which the state is itself released from the need to cover the balance-of-payments deficit in gold, this eliminates the incentive for the authorities deliberately to withdraw the excess money supply and reduce the credit facilities in the country. Rueff believes that such a course of development could help to restore the disrupted balance-of-payments equilibrium. He has very aptly called the balance-of-payments deficit covered through short-term external indebtedness as a "deficit without tears".

He believes that another consequence of the gold-exchange standard is the exploitation to which the reserve currency countries subject the countries whose currencies have no international status. Thus, the US balance-of-payments deficit resulted from the Americans' buying real values (land, plants, enterprises, banks and other financial institutions) on the territory of other capitalist countries and making government expenditures for their military and political purposes. It turned out that these countries accumulated US "spectral liabilities" and themselves financed US expenditures. This, says Rueff, "enables the United States to live at the expense of its suppliers", and calls it a "system of plunder that is unprecedented in history".[1] At the same time, the countries accumulating dollar reserves as a result of their balance-of-payments surplus were forced to put into circulation additional amounts of their currencies to "secure" these assets. This intensified inflationary processes in these countries and stimulated the growth of prices.

Finally, Rueff's third effect was the erosion by these processes of the whole capitalist international monetary system. The growing accumulation of British and US short-term external liabilities, Rueff believes, made the reserve currencies unstable and eventually produced the prospect of a collapse of the whole credit pyramid based on the US gold stock, and a world monetary crisis. This, for its part, is fraught with the danger of an economic crisis, with falling industrial output and growing unemployment.

But what are the recipes for curing the monetary disease suggested by those who accept Rueff's views? They say that only the free movement of gold between countries will keep world economic exchange in equilibrium and make for unhampered international settlements. Of course, they realise that in the present conditions it is impossible to restore the gold standard in its "classic" forms, but they urge the creation of a mechanism in the capitalist world that could be called an "interstate gold standard".

Accordingly, Rueff has proposed that the cap-

[1] Jacques Rueff, *Le Péché Monétaire de l'Occident*, p. 264.

italist countries should conclude an international convention with the following commitments:

> "a) an increase, from a given date, in the price at which the participating countries buy and sell the yellow metal (either directly or through the medium of the dollar);
>
> "b) a solemn confirmation by all the holders of monetary balances (dollar-balances, sterling-balances, and, in certain cases, franc-balances) that they will be able, if they so desire, to obtain reimbursement on demand in the yellow metal or in exchange at rates under the new parity of the credit instruments they hold;
>
> "c) an offer to countries whose metallic reserve, even after its revaluation, has proved to be inadequate in meeting possible demands for a reimbursement of their short-term liabilities, of gold loans within the established limits by countries in possession of gold but without balances to reimburse, with the amount of these loans being deducted from the increase in nominal value resulting from parity changes;
>
> "d) a commitment by the participating countries—in order to avoid a fresh running-up of monetary balances—to issue money in the future only against assets in gold or national currencies but not against foreign exchange. Such a commitment would simply signify a return to the system anterior to the establishment of the gold-exchange standard."[1]

Consequently, according to Rueff's project (points *b* and *d*), the capitalist countries, on the one hand, will be able at any time to convert their foreign-exchange assets into gold, and on the other, will be in a position in which they will be forced, in

[1] Jacques Rueff, *op. cit.*, p. 243.

practice, constantly to do so. This proposal is designed to set up an order in monetary relations under which the accumulation of large short-term liabilities by some countries with respect to others would henceforth prove to be impossible.

Rueff believes that the main purpose of raising the monetary price of gold (point *a*) is to enable the reserve-currency countries (i.e. the United States and Britain) to meet their accumulated external short-term international liabilities in gold. Finally, Rueff's proposal on gold loans to each other (point *c*) is designed to ease the acute maldistribution of the gold stock in the capitalist world.

Present-day advocates of the metallic approach to international monetary relations think that the re-establishment of the necessity for all countries to cover their balance-of-payments deficit in gold creates an incentive inducing the authorities to withdraw excess money supply and, accordingly, to reduce the aggregate purchasing power, and also to shrink the credit facilities and access to loans in the country, as they did under the former gold standard. They believe that this will tend to lower prices and so help to restore the disrupted balance-of-payments equilibrium.

Rueff has reached the following conclusion:

> "So long as the convertibility of currencies (into gold—*D.S.*) is not restored, the world will remain doomed to a disequilibrium of balances of payments, unreliable currencies, disorderly flows of capital, instability of exchange rates, and all manner of disorders resulting from the ignorance of men and the impotence of institutions."[1]

One must say that a tangible increase in the price of gold with respect to the capitalist currencies would indeed for a time really ease the mone-

[1] Jacques Rueff, *op. cit.*, p. 281.

tary difficulties of world capitalism. The re-establishment to this or that extent of gold in its former role in international settlements among the capitalist states would evidently put some curbs on the external economic and political expansion of US imperialism and arbitrary acts by the most powerful capitalist countries in the monetary sphere. But as Karl Marx showed, even in its heyday, the gold-standard mechanism was unable reliably to rid the capitalist countries of disequilibrium in their external payments. It is even less capable of doing this in the present epoch of state-monopoly capitalism and the general crisis of the capitalist system, when a tremendous influence is exerted on balances of payments by the chaotic flows of capital from one country to another and the foreign military policy expenditures of the imperialist states which have assumed unprecedented proportion. The level of this spending fails, in practice, to respond to the operation of the price mechanism which, the "metallists" believe, is set in motion by the influx and outflow of gold.

Besides, in the present conditions it is highly improbable that the gold standard could be re-established, if only in relations among countries. With the present level of integration processes in the world capitalist economy, the internationalisation of production and exchange, and the tremendous disequilibrium in economic exchange between countries, the existing gold stock cannot meet the requirements in international payments instruments. That being so, the prevailing notion in the capitalist world is that the mechanism is not flexible enough, and that it narrows down the framework of economic and political manoeuvring by capitalism in the world arena.[1]

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[1] In this context, one financial journal has written about the plans for restructuring the capitalist monetary system on the basis of Special Drawing Rights:

"Gold could only have a declining role in this scenario...

This will also be seen from the fact that the leading Western countries have agreed to abolish the official price of gold. The draft of a new IMF charter (agreed at the Jamaica conference) does not contain any formulas testifying either to a recognition or a denial of gold's role as an international reserve asset. Accordingly, the agreement is seen in the West, especially in the United States, as official demonetisation of the yellow metal, stripping it of its monetary functions in international commerce.

At the same time, the current upheavals in the world capitalist monetary mechanism and the sharp aggravation of the interimperialist contradictions have produced a counter-trend towards a certain re-establishment of gold in its lost positions within the mechanism of international settlements. The explanation will be found in the fact that this situation, involving a growth of nationalistic aspirations in the external economic policy of the capitalist states, relatively worsens the conditions for using credit instruments in external payments, for these require mutual trust and international coordination of economic behaviour. Accordingly, there should be a growing tendency to rely in international settlements on "cash", i.e. on the precious metal.

Thus, for instance, one is left with the impression that having agreed at the Jamaica session to the official demonetisation of gold, France has not abandoned its plans to keep for it de facto the role

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It was considered unsuitable as the primary reserve asset of the system because the value of the world's gold reserves could only keep pace with the increasing value of world trade by periodic increases in its price. Moreover the price in the free market was already subject to erratic changes due to speculative demand and uncertainties about the supply. With a highly volatile price it could neither be a good store of value nor a convenient unit of account." (*The Banker*, London, January 1975, p. 2.)

of an international reserve and payments medium. An analysis of France's approach warrants the conclusion that its ruling circles have been trying to direct developments towards a growing importance of the capitalist countries' gold reserves.

The present legalisation of the market price of gold and the revaluation on that basis of the price of the gold stock held by the central banks in the Western countries tangibly enhance the weight of the gold component in international liquidity resources and improve the monetary positions of countries which have relatively large stocks of gold.

What is also highly characteristic is that, in accordance with the Jamaica agreement, the central banks of the capitalist countries are able freely to buy gold on the private market at the prevailing prices (they were given the right to sell gold back in 1973). Some of the central banks (the French in particular) have already used this opportunity. If the situation does indeed arise in which countries that have accumulated foreign-exchange reserves that are excessive from their standpoint will convert a part of these reserves into gold, while states with balance of payments in deficit will, on the contrary, sell gold for foreign exchange, such a situation would be characterised as at least a partial re-establishment of the role of gold as an international payments medium.

But the idea of establishing an interstate gold standard to its full extent would clash with the objective long-term processes in the world capitalist economy, including the growth of international interdependence of capitalist production, the progressive interlacing of the individual countries' economic organisms, and the continued expansion of the sphere of international state-monopoly regulation in the capitalist world.

4. The Neo-Keynesian Approach: Internationalisation of the Monetary Mechanism

Bourgeois economists who continue to take the Keynesian view of international monetary problems rely on the concept of putting the balance of payments into equilibrium, a concept worked out by Keynes and his followers. They have also sought to modernise, in the light of present conditions, Keynes's proposal for regulating the capitalist countries' international monetary relations.

The Keynesian concept of external payments equilibrium is based on Keynes's theoretical conclusions which he set out in his chief work, *The General Theory of Employment, Interest and Money*, in which he revised the "outdated" quantity theory of money. In contrast to his predecessors, Keynes went beyond the traditional notion that money supply should be contrasted only to commodity prices, and suggested that there was an interdependence between money supply and "effective demand", on the one hand, and output, the degree of use of productive resources, and employment, on the other. It is this important element of Keynesian economic doctrine (i.e. inclusion in the analysis, alongside the money and price mechanism, of the sphere of production in which income is shaped) that produced the new view of the way payments balances were set right. The chief force, which eventually re-established the equilibrium in the international payments turnover, is not the movement of prices in connection with changes in money supply, but changes in the level of business activity, employment, and income which have a direct effect on the state of foreign trade. This force is automatically set in motion by the same factors which disturb the balance of external payments and cause the outflow or influx of gold. Metzler wrote:

> "The essence of the new theory is that an external event which increases a country's exports will also increase imports *even without price changes*, since the change in exports affects the level of output and hence the demand for all goods. In other words, movements of output and employment play much the same role in the new doctrine that price movements played in the old."[1]

The Keynesian concept of international monetary circulation appears to be more realistic than the theories of 19th-century bourgeois economists, but it is, in fact, an apologetic one, because it obscures the antagonistic contradictions of the capitalist mode of production, international economic exchange and monetary circulation in the capitalist world. Cyclical fluctuations in the economic situation, crises of overproduction, the uneven and leap-frogging development of the capitalist countries, and the acute upheavals arising from the general crisis of capitalism, all of these make it impossible for the West to maintain an external economic equilibrium, whether through an incomes mechanism or a price mechanism.

Besides, the Keynesian concept of balance-of-payments equilibrium turned out to clash with the "general theory of employment", whose purpose was to rid capitalism of devastating economic crises and reduce unemployment which causes bitter social conflicts and political upheavals that jeopardise the very existence of the capitalist system. The model Keynes presented in his *General Theory* is, in effect, a normative one, for it starts from a preset level of employment (and a corresponding rate of income) with the quantitative parameters of the basic instruments of economic

[1] L. A. Metzler, *Collected Papers*, 1973, p. 4.

policy serving as endogenic output variables. According to this theory, the instruments and means of government anti-crisis policy include: reduction of interest rate; expansion of money supply; stimulation of effective demand; and increase in government investment.

It is also based on the assumption of a self-correcting process of external economic exchange and payments turnover, which is why it inevitably assumes that the framework for realising anti-crisis policy is much too narrow. After all, when a deficit develops on the balance of payments, the authorities are forced to take steps of the very opposite nature, namely, to increase interest rate, to limit money supply, to restrain market demand, and reduce government spending, so as to halt the dangerous outflow of gold. From this it follows that balance-of-payments equilibrium is achieved precisely through a reduction in industrial output and an increase in unemployment.

Consequently, the Keynesian explanation of the mechanism by means of which payments balances are evened out did not eliminate the contradiction between the need for external equilibrium, on the one hand, and the internal economic and social conditions, on the other, a contradiction that was incorporated in the bourgeois concept in the 19th century. What is more, the Keynesian logic itself suggested the need to recognise that this contradiction was becoming ever deeper and more acute.[1]

[1] The Keynesians are themselves forced to admit that their mechanism is internally incoherent and clearly not effective enough to keep external economic ties in stable equilibrium. Consider the following remark by Metzler: "In the modern view, a country with a deficit in its balance of payments is likely to eliminate this deficit, in part at least, through a low level of income and employment. The conflict between domestic stability and international equilibrium, which has long been a familiar part of classical monetary theory, is thus shown to be much more important than had formerly been supposed. In an unstable world, the choice confronting an individual country is not merely be-

In search of ways to overcome the contradiction between the requirements of internal and external equilibrium, Keynes turned to international liquidity, and put forward the idea of a "regulated or administered currency" for international payments in the capitalist world, and the formation, through mutual credit support, of a buffer stock of international liquidity instruments available to the capitalist countries. The use of these is designed to provide each country with an additional time limit in the course of which the balance of payments could be restored to equilibrium without any sharp disruptions simultaneously occurring in internal equilibrium, i.e. unemployment and underloading of productive capacities.

This was expressed in the most practical terms in Keynes's proposal, at the end of the Second World War, to establish an International Clearing Union based on international bank money and called "bancor", a proposal which appeared to provide a roof for the edifice of Keynes's general macroeconomic theory.

Keynes argued along the following lines:

> "Just as the development of national banking systems served to offset a deflationary pressure which would have prevented otherwise the development of modern industry, so by extending the same principles into the international field we may hope to offset the contractionist pressure which might otherwise overwhelm in social disorder and disappointment the good hopes of our modern world. The substitution of a credit mechanism in place of hoarding would have repeated in the international field the same miracle,

tween price stability and international equilibrium, as envisaged by the classical theory, but between stability of employment and international equilibrium." (L. A. Metzler, *Collected Papers*, pp. 12-13.)

already performed in the domestic field, of turning a stone into bread."[1]

The neo-Keynesian line in international monetary problems is most circumstantially represented in the works of the US economist Robert Triffin.[2] When explaining the causes of the current crisis of the capitalist monetary system, Triffin, in effect, describes the same processes in the monetary sphere which were pointed out by Rueff. There is, however, an essential distinction between the neoliberal and the neo-Keynesian criticism of the Bretton Woods monetary system.

First, the neoliberals believe that the weakest spot of the system is the extensive use in international commerce and excessive accumulation by countries of paper money as against gold, i.e. they charge that it is "too Keynesian", while the Keynesians say that it is the inadequate development and centralisation of the paper-money component of international liquidity, and the too intimate ties with the national soil of the individual countries. So, it is "not Keynesian enough".

Second, the neoliberals regard the postwar monetary mechanism above all as a powerful generator of inflation in the capitalist world, especially beyond the boundaries of the reserve-currency countries, while the neo-Keynesians emphasise the existing

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[1] *Proposals for an International Clearing Union*, Cmd. 6437, HMSO, London, 1943, pp. 11-12. By "miracle" he meant the elimination or easing of the crisis upheavals through a broad development of a credit system, a clear case of wishful thinking.

[2] See: Robert Triffin, *Gold and the Dollar Crisis. The Future of Convertibility*, Yale University Press, New Haven, 1961; also his: *The Evolution of the International Monetary System: Historical Reappraisal and Future Perspectives*, Princeton University, Princeton, New Jersey, 1964; *The World Money Maze. National Currencies in International Payments*, Yale University Press, New Haven-London, 1966; *Our International Monetary System: Yesterday, Today and Tomorrow*, Random House, New York, 1968.

or, at any rate, potential shortage of international liquidity, with accent on the deflationary or stagnation effect of this mechanism, mainly for the reserve-currency countries.

When assessing the main components of capitalist international liquidity today, Triffin also lays down a strategic line for the possible restructuring of the monetary system that differs from Rueff's. First of all, he rejects the prospect of a return to gold as the basis of international liquidity reserves: "Gold has long ceased to provide adequate amounts of international liquidity for an expanding world economy." Nor does he believe that it is possible to keep reserves for external payments in national currencies as a supplement to gold because this "cannot fail to increase further and further the vulnerability of the world monetary system to shifts of confidence ... in the national currencies actually used as reserve media." He says that

> "the use of *national* currencies as *international* reserves constitutes indeed a 'built-in de-stabiliser' in the world monetary system." That being so, "the logical solution of this dilemma would lie in the 'internationalisation' of the foreign exchange component of monetary reserves".[1]

Triffin believes that the most important component of monetary reform should be "a system of reserve creation and management, adjusting the total levels of reserves to world needs and making use of them for internationally agreed objectives."[2] Accordingly, he proposes a pooling of the present surplus dollar and sterling reserves of the capitalist countries, their IMF limits for "conventional" foreign exchange credits, and their SDR (special drawing rights) reserves into a single type of asset, namely,

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[1] Robert Triffin, *Gold and the Dollar Crisis*, p. 87.
[2] *The Times*, September 13, 1971, p. 21.

reserve deposits at the IMF. These would substitute for deficit gold and act as a "sensitive instrument for the accumulation of reserves."

Since IMF deposits are expressed in gold units, there is no risk of their depreciation, like that of national currency reserves, says Triffin. The holders of IMF deposits also need have no fear of their assets being blocked, because the IMF guarantees their unhampered use for payments by all member countries.

> "These provisions should make it possible for all countries to count their balances with the Fund as a normal and valuable component of their monetary reserves, and as fully equivalent to gold.[1]

Triffin's proposals suggest that in determining the composition of their reserves for external payments, the countries would deal with two quantitative restrictions:

first, they would not be able to increase their reserves in the national currencies of other states above a definite ceiling (say, 15 per cent of the total reserves); and

second, they would have to hold at least 20 per cent of their total reserves in the form of reserve deposits with the IMF, being free to choose between gold and IMF deposits for the rest of their international liquidity.

It is Triffin's assumption that the liabilities of the present reserve-currency countries accumulated over the period of the gold-exchange standard would be consolidated in permanent loans ("consols") belonging to the IMF, with the United States and Britain providing guarantees of a stable exchange rate and paying an interest to the IMF. These liabilities would have to be covered by the debtor countries chiefly from their future active

[1] Robert Triffin, *Gold and the Dollar Crisis*, p. 105.

balances in external payments, whenever the formation of these active balances pushes their total reserves above an agreed "normal" level.

Triffin emphasises that his proposals "preserve the core of the Keynes Plan mechanism".[1] But he sets out to "improve" the plan by modernising those of its aspects which had been most criticised by the ruling circles of the United States and some other countries, and which caused it to be rejected. Triffin believes that the most vulnerable spot of the Keynes Plan is the danger that credit operations by an international monetary institution could exert an intense inflationary influence on the world capitalist economy.

How does Triffin propose to neutralise the potential inflationary effect of the IMF's credit activity? He says that the most important and practical means for doing this is direct restriction of credits (made available by the IMF to its members for a period of 12 months) to a sum-total which, together with the annual growth in the monetary gold reserve, would increase the total world reserves by 3-5 per cent a year. The same purpose would be served by the right extended to IMF countries for freely converting into gold the assets listed on their IMF deposits, if they are in excess of the mandatory minimum.

Let us emphasise that Triffin's arguments in favour of his plan tend to run in a circularity of typical Keynesian notions concerning the mechanism of balance-of-payments equilibrium, and the nature and functions of the capitalist countries' international liquidity reserves. The key role in these notions is the premise that in response to the disruption of the balance-of-payments equilibrium a protective reaction will spontaneously emerge within the country's internal economic organism. Still, like Keynes, Triffin does not believe

[1] Robert Triffin, *op. cit.*, p. 103.

that the capitalist economy should be left alone to face the destabilising impulses generated by external economic and payments upheavals.

> "The total surrender of national sovereignty by member countries over all forms of trade and payments restrictions, and even over exchange rates ... in favour of a mere nineteenth century *laissez faire*, unconcerned with national levels of employment and economic activity" is utterly inconceivable today.[1]

Considering that the gold standard was the cornerstone of the *laissez faire* system, one will easily understand why, in contrast to Rueff, Triffin takes a sharply negative view of the international functioning of gold. His plan provides that the central banks would keep their present gold reserves until the time the new system comes to enjoy full confidence, and that in the future they would realise a surplus of these in an orderly manner on the world's private gold market. Meanwhile, deficit countries holding gold above the average proportion to total reserves could be required to use a part of their gold for payments via the IMF to surplus countries with a lower proportion of gold in total reserves.

Consequently, Triffin's idea is that the capitalist world's acute monetary problems should be solved through a radical internationalisation of the monetary mechanism.

However radical such neo-Keynesian efforts may appear, they cannot eliminate the fundamental contradictions of capitalist monetary and financial relations or make the international monetary mechanism stable and reliable.

Indeed, all neo-Keynesian works are keynoted by the idea that the free rivalry between gold and the new liquidity instruments (IMF deposits)

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[1] *Ibid.*, p. 146.

will end with a victory for the latter and that gold will be completely ousted from the world monetary mechanism, leaving IMF deposits the only instrument of external payments ensuring a final settlement of outstanding international liabilities.

But Triffin has nothing persuasive to say about how his goal can be achieved. One can hardly view seriously his reference to the fact that IMF deposits will yield an interest to their holders, while the possession of gold yields no such thing. Bank accounts and investments in present-day reserve national currencies also yield a definite income, but that has not prevented the conversion of a part of them into gold, or, at any rate, an urge to do so.

At the same time, Triffin ignores or presents in a distorted light some of the key features of the world capitalist economy today. Their objective analysis shows that his hopes are illusory and utopian, and that the pivotal idea of his plan is unworkable.

Consider the following points.

First, Triffin and other bourgeois economists who take the same view clearly exaggerate the role of the gold-exchange standard in the development of the inflationary process in the capitalist countries. That process is based on internal factors like deficit financing of nonproductive, especially military, expenditures by the bourgeois governments and inflation of prices by the monopolies in their drive to maximise profits. However substantially the monetary system is restructured, it can never eliminate the basic factors behind the inflation in the capitalist world. That is why IMF deposits will be depreciated just as national paper money is being depreciated in the capitalist countries today. Hence the prospect of a devaluation of IMF deposits with respect to gold, or transition to a "floating" market price for gold, which will induce the monetary agencies of the IMF countries to convert their foreign-exchange deposits into gold, so returning to square one.

Second, the Keynesians are not right in putting on the gold-exchange standard the whole blame for the sharp and protracted disruptions of the international payments equilibrium in the capitalist world, while ignoring the real and deeply rooted causes like the anarchy of capitalist production which keeps producing sharp shifts in the balance of strength between the individual imperialist powers; economic crises stemming from the antagonistic contradictions of the capitalist mode of production; the ungoverned export of capital by the multinational monopolies in their drive to maximise profits; the chaotic movements of vast masses of "hot money" from one country to another; the fabulous government spending abroad for military and political purposes, all of which are factors connected with the ever deepening general crisis of world capitalism. Quite obviously these phenomena, which are intrinsic to the capitalist economy today, are not affected by any restructuring of the monetary mechanism.

That being so, there is no real prospect in the foreseeable future for an effective mechanism to keep the economic and payments exchange between the capitalist countries in equilibrium. And so long as there is no such mechanism, it is hard to imagine how the West will get rid of a medium of final international settlements which, itself being a product of labour, would be a material vehicle of value. Gold evidently continues to be the commodity best suitable for this role even today, although there is certainly a trend in the capitalist world to demonetise it.

Finally, the third point is that Triffin, who makes the unwarranted assumption that the monetary agencies of the capitalist countries will behave in a "reasonable" way, exaggerates, for apologetic purposes, the potentialities and effectiveness of state-monopoly regulation of monetary relations.

The world capitalist economy is an aggregation of national economies with their specific economic and social conditions. In accordance with the law formulated by Lenin, the capitalist countries' development is extremely uneven and erratic. That being so, joint action to regulate the monetary sphere inevitably goes to sharpen the whole set of economic, social and political antagonisms.

Because of these contradictions, the highly acute problem of international liquidity was not solved by the Jamaica agreement either. The draft of the revised IMF Charter contains a statement of intent to turn SDR into the chief instrument of settlements between central banks and, accordingly, the chief reserve asset of the international monetary system. This, however, is not backed up with sufficienty clearcut practical propositions to ensure its realisation. One could say, therefore, that a restructuring of the system of aggregate international reserves through their unification on the basis of an international reserve asset like SDR is being put off indefinitely.

5. The "Monetarist Counter-Revolution" and "Floating" Exchange Rates

Milton Friedman, the most active champion of "floating" exchange rates, set forth his arguments in a number of works written since the 1950s.[1]

[1] Milton Friedman, "The Case for Flexible Exchange Rates". In: *Essays in Positive Economics*, The University of Chicago Press, Chicago, 1953, pp. 157-203. Reprinted in: *Foreign Trade and Finance*, Ed. by William R. Allen and Clark Lee Allen, the Macmillan Company, New York, 1959, pp. 313-347; Milton Friedman, Robert V. Roosa, *The Balance of Payments: Free Versus Fixed Exchange Rates*, American Enterprise Institute for Public Policy Research, Washington, 1967; Milton Friedman, *How Well Are Fluctuating Exchange Rates Working?* Reprint No. 18, American Enterprise Institute, Washington, October 1973.

Friedman and his followers take the monetarist doctrine as the basis for their approach to international monetary relations, external economic trade equilibrium, and practical recommendations for a mechanism to correct payments balances. They make two pivotal assertions.

First assertion: they say, as Keynes did, that there is a clearcut connection between money supply, on the one hand, and the price level and the use of productive resources (labour force, means of production and raw materials), on the other; but in contrast to the Keynesian view, they say that the connection between these three parameters is "rigid", so that a change in money supply results not in a consecutive, but in a simultaneous change in price level and use of resources. Thus, an expansion of money supply to increase employment directly results in a growth of prices, while a reduction in prices through a reduction in money supply can be achieved only through an increase in unemployment.

Second assertion: arbitrary changes by government agencies of money supply and aggregate effective demand by means of discount, fiscal and other methods, under the impact of current market fluctuations, have a destabilising "disruptive" influence on the capitalist economy.

From these assertions it follows that manipulation of internal prices and incomes cannot be used as a means for evening out the balance of payments.

Friedman analysed two main aspects in the use of this method.

The first was the functioning of the price mechanism in which bourgeois political economy in the 19th and early 20th centuries sought to find an explanation of the processes of external economic balancing. He drew attention to the fact that this mechanism could function only on one imperative condition: the flexibility of domestic prices. But, in his opinion (and here one could agree with him), in the capitalist world today this condition is totally absent. Indeed, prices are highly inflexible or are flexible in a one-sided manner: they are more capable of rising than of falling.

The other aspect considered by Friedman is the functioning of the income mechanism, which is the basis of the Keynesian model for balance-of-payments regulation. In accordance with his theoretical views, Friedman, like Keynes, holds that the effect of the impulses generated by monetary policy is not confined to the sphere of the price mechanism but ripples through to the sphere of production, employment, and income. According to Friedman, the key role in this rippling process is that wages are among the "least flexible prices", so that the inability of wages to decline when other prices do is compensated by a reduction in demand for labour by employers.

Let us recall, however, that the Keynesians ultimately see no other real possibility for maintaining external payments flows in equilibrium except through a mechanism for changing internal income which is stimulated by means of an appropriate discount and fiscal policy. But Friedman draws the conclusion that the price the economy has to pay for this is much too high:

> "This is clearly a highly inefficient method of adjusting to external changes. If the external changes are deep-seated and persistent, the unemployment produces steady downward pressure on prices and wages, and the adjustment will not have been completed until the deflation has run its sorry course."[1]

The only possible alternative, according to Friedman, is regulation of the balance of payments through changes in the exchange rate. The neo-

[1] Milton Friedman, "The Case for Flexible Exchange Rates". In: *Foreign Trade and Finance*, New York, 1959, p. 321.

classics assert that the maintenance of constant exchange rates through government intervention in the monetary markets deprives the international settlement system of the necessary flexibility and makes it too rigid. In this context, Friedman wrote:

> "Whatever may have been the merits of this system for another day, it is ill suited to current economic and political conditions... There is scarcely a facet of international economic policy for which the implicit acceptance of a system of rigid exchange does not create serious and unnecessary difficulties."[1]

The mechanism by means of which the exchange rate exerts an influence on the balance of payments is sufficiently well known. When country A runs up a deficit on its balance of payments, it lowers the exchange rate of its currency. The result is that its goods become relatively cheaper for foreign buyers when their prices are expressed in foreign currency at the new rate, even if there has been no change in the domestic prices of these goods in the national currency. This produces a trend for an increase in the exports of country A. Meanwhile, the prices of foreign goods expressed in the national currency of country A now turn out to be relatively higher for its buyers, although in the producer countries they had not changed at all in terms of their national currencies. Hence, a reduction in imports. The expansion of exports, on the one hand, and the reduction in imports, on the other, eliminates or, at any rate, reduces the excess of foreign payments over receipts by country A.

Where there is a surplus on the balance of payments, events tend to run in reverse: because of

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[1] *Ibid.*, pp. 313-314.

the higher foreign exchange, exports from this country become more expensive for foreigners, and imports, relatively cheaper for domestic buyers, in consequence of which there is again a trend to eliminate the balance-of-payments disequilibrium (in this case, the excess of foreign receipts over payments).

Friedman prefers changes in the exchange rate as the way to maintain balance of payments equilibrium, but objects to this being done by government agencies. This means only one thing: exchange rates freely fluctuating under the influence of supply and demand. Indeed, Friedman asserted that flexible or floating exchange rates taking shape freely on the open market chiefly as a result of private transactions and changing daily like other market prices are absolutely essential for

> "our basic economic objective: the achievement and maintenance of a free and prosperous world community engaging in unrestricted multilateral trade. ... Liberalization of trade, avoidance of allocations and other direct controls both internal and external, harmonization of internal monetary and fiscal policies—all these problems take on a different cast and become far easier to solve in a world of flexible exchange rates and its corollary, free convertibility of currencies."[1]

Friedman warns against the possibility of "dirty floating" of exchange rates, by which he means intervention (even if on a more limited scale than under the system of fixed exchange rates) by government agencies in the functioning of the monetary market.

What then are the merits and advantages of freely fluctuating exchange rates?

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[1] Milton Friedman, "The Case for Flexible Exchange Rates", *op. cit.*, pp. 313-314.

Friedman considers two possible situations.

First: there is a prevalent conviction on the money markets that the disruption in a country's balance-of-payments equilibrium is temporary and transient, and that soon the movement of the exchange rate will be reversed. In that case, those involved in monetary transactions—exchange speculators (be it citizens of this or any other country) have a tendency to change the size of their deposits in the currency of this disequilibrium country in such a way as to exert a moderating influence on the movement of the exchange rate. Thus, when the exchange rate of any currency rises, the holders of this currency are induced to sell some of their assets in this currency (while its price is high) for another currency: later, they will be able to repurchase the initial currency, but at a lower price, which gives them a margin of speculative profit. Conversely, a fall in the exchange rate is an inducement to buy the currency concerned with a view to its subsequent resale at a higher price.

Thus, in contrast to the system of rigid exchange rates, when speculation has a clearly expressed destabilising character, under the freely fluctuating exchange rate mechanism, Friedman asserts, such "speculative" deals (by using the word in quotes he gives it a positive meaning) in fact provide the country with monetary means covering the temporary surplus balance or compensating for the temporary deficits on the balance of payments. Friedman says:

> "In my opinion ... the market will do a far better job of speculation in exchange than the government."[1]

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[1] Milton Friedman, *How Well Are Fluctuating Exchange Rates Working?*, p. 5.

In the other situation, there is a prevailing conviction on the money markets that changes in the exchange rate are constant and irreversible, because they have been caused by the underlying economic conditions. Friedman believes that in such circumstances the inducement to buy and sell exchange will be the opposite of that described above: in the event of a deficit on the balance of payments in any country, its currency will be sold, and in the event of a surplus, purchased. This will accelerate the decline or rise of the exchange rate, and so carry it closer to the final point at which the balance of payments equilibrium is re-established.

The neoclassics, including the monetarists, assert that by intensifying the spontaneous operation of the market mechanism in shaping exchange rates it would be possible to eliminate the influence of disruptions in the equilibrium of external economic exchange on the course of capitalist reproduction, more reliably to secure the automatic maintenance of payments balances in equilibrium and a relatively painless adaptation of the individual economies to the constantly changing situation on the world capitalist market.

The monetarists believe that the main objective of economic policy is to maintain internal monetary stability, which means prevention both of inflation and of deflation. But Friedman points out that with rigid exchange rates and without trade and monetary restrictions no country can attain that objective unless every other big country with which it is directly or indirectly linked through trade follows the same line. Hence the need to achieve "harmonisation" of internal monetary policies of the individual capitalist countries.

Friedman holds that this would call for an international authority to control the issue of money in each country, but he is not sure that it is "desirable that such far-reaching powers be surrendered to any authority other than an effective federal government".[1] That is another important distinction between Friedman's concept and that of the Keynesians, who want the broadest possible inter-state regulation of monetary and financial relations.

Friedman believes that the system of fluctuating exchange rates does away with the need for such burdensome coordination of internal monetary and fiscal policies and enables each country to pursue its own policy in ensuring internal monetary stability. If, for example, under such a system any country goes in for inflation, that will inevitably depreciate its exchange rate. This neutralises the influence of internal inflation on the international trade positions of such a country and relaxes or eliminates the trend to a transfer of inflation to other countries. Friedman sums this up as follows:

> "In effect, flexible exchange rates are a means of combining interdependence among countries through trade with a maximum of internal monetary independence; they are a means of permitting each country to seek for monetary stability according to its own lights, without either imposing its mistakes on its neighbours or having their mistakes imposed on it."[2]

Finally, the monetarists assert that the floating exchange-rate mechanism has a built-in shock-absorber ensuring an optimal pace and duration of final adaptation by the capitalist economies to changing external economic conditions (this entails a re-allocation of production resources and a restructuring of the composition of commodities designed for consumption and investment). They say that this is done by the "stabilising speculation", which was considered above. They believe

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[1] Milton Friedman, "The Case for Flexible Exchange Rates", p. 343.
[2] *Ibid.*, p. 344.

that this, in effect, means that the speculators extend a loan to the country whose currency is being depreciated. From the monetarists' standpoint, this mechanism produces the same effect as direct crediting through government channels: covering of its balance-of-payments deficit (through loans) by the country whose currency is being depreciated, or, conversely, compensation (through credits to foreign countries) by the country whose currency is being appreciated of its surplus on external account. This device helps to avoid the extremes both of immediate adaptation only through a movement of exchange rates, and avoidance of the need to restructure the economy in accordance with the changing conditions. That is why the self-regulation of payments balances through a fluctuation of exchange rates should substantially reduce the capitalist world's requirements in international liquidity.

That is yet another point of distinction between the neoliberal and the Keynesian approach, which provides for recourse to external credits in order to win time.

What has been said shows that the floating exchange-rate concept is a direct application to international monetary and financial relations of the basic theoretical constructs of the neoclassics, the monetarists in particular. In this context, Friedman claimed that flexible exchange rates are a logical continuation in the international sphere of the monetary and financial structure, i.e. the monetarist recipes, which ensure economic stability.

Before getting down to an analysis of this concept, one has to say that the mechanism of state-monopoly regulation of international monetary relations based on Keynesian notions is now indeed in deep crisis, but abandonment of interstate regulation and establishment of exchange rates freely fluctuating under the impact of market forces do not hold promise of release from monetary upheavals in the capitalist world either. After all, the antagonisms of the world capitalist economy are fuelled precisely by the haphazard play of market forces, the forces on which the neoclassics pin their hopes.

One could agree that spontaneous changes in exchange rates (in response to disruptions of balance-of-payments equilibrium) could in some cases generate a tendency to restore equilibrium, but the floating exchange-rate system makes the sharply fluctuating rates unstable and, as the record shows, "stabilising speculation" provides no more than a flimsy basis. A more realistic assumption is that speculation with freely fluctuating exchange rates must be destabilising, which means that when the exchange rate of a currency falls, speculators do not buy but continue to sell it, and conversely, when the rate rises, they do not sell, but continue to buy. Some Western economists have analysed empirical data from the inter-war period to show that destabilising speculation prevails under floating exchange rates.

Friedman admits that flexible exchange rates would increase the uncertainty concerning their behaviour. He asserts, however, that a flexible exchange rate need not be an unstable exchange rate.

> "If it is, it is primarily because there is an underlying instability in the economic conditions governing international trade."[1]

That is true, but one has to add also that the operation of the law of the uneven and erratic development of the world capitalist economy and the steady deepening of the general crisis of the capitalist system tend to produce more than enough causes for a constant reproduction of this "underlying instability".

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[1] Milton Friedman, *op. cit.*, p. 328.

Meanwhile, stable exchange rates are ever more important for the world capitalist economy, with its steadily growing international division of labour and closely interwoven economies. The increasing uncertainty over the possible changes in exchange rates increases the risk of exchange losses and makes imperative burdensome hedging operations on forward markets, hampers international comparisons of production efficiency for various types of goods, and this to some extent works against the development of world trade and other international economic relations.

Friedman claims that the greater uncertainty over the behaviour of exchange rates in the absence of intervention in the money markets is a kind of price that has to be paid for ensuring the stability of the internal economic mechanism, but that is a highly vulnerable claim. The record shows that a decline in freely fluctuating exchange rates caused by a country's tendency to build up a deficit on its balance of payments in some cases results in a growth of inflation in that country.

As the exchange rate falls, the prices of imported goods expressed in that currency turn out to be higher than those before the decline in the rate, and the increase in prices for imported goods (especially raw materials and semifinished products) which are used to make goods in that country, ripples through the costs to the prices of the latter, so eventually leading to a general rise in the level of prices in that country. This may produce a situation in which the mechanism that was to have eliminated the balance-of-payments deficit, which initially caused the decline in the exchange rate, will not work. In such circumstances, the maintenance of the deficit brings about a new decline in the exchange rate, which for its part starts the next round of the "inflationary slide".

Furthermore, a change in the relation of prices in the local and foreign currencies, resulting from the movement of the exchange rate, does not yet mean that this will be automatically followed by a change in the volume of exports and imports on a scale leading to a re-establishment of equilibrium on the trade and payments balances. The fact is, for instance, that a rise in the competitiveness of goods caused by a decline in the exchange rate may be to some extent neutralised by a low elasticity of exports, i.e. industry's inability markedly to increase the manufacture of goods for export. Similarly, a reduction in the prices of foreign goods caused by a rise in the exchange rate may or may not increase imports (when, say, the economy is in a phase of stagnation it may prove to be incapable of absorbing the additional quantities of imported products).

We find, therefore, that this concept shares the common defect of bourgeois economics, which tends to exaggerate the role of the sphere of circulation and underrate that of material production.

Under the general crisis of world capitalism, some imperialist countries (the United States and Britain, in particular) have increased their foreign spending to tremendous proportions by pursuing foreign policies designed to resist the people's struggle for national liberation and social emancipation (the maintenance by the leading capitalist countries of armed forces and military bases abroad, subsidies and credits to pro-imperialist regimes, etc.). With freely fluctuating exchange rates, the chronic deficits on their balance of payments owing to such spending must automatically press down their exchange rates. Falling exchange rates, for their part, should make their goods more competitive and, in consequence, expand exports and constrain imports, a process that will run until a surplus in the foreign trade sector of the total balance of payments equalises the deficit in the sector of the government's external financial operations in political and military matters. This may carry foreign trade expansion to such proportions that it will do grave harm to other countries, causing a decline in production, business bankruptcies, ruin of small producers, and a sharp aggravation of social contradictions.

Consequently, floating exchange rates turn out to be an instrument used by the leading imperialist powers to shift the burden of their governments' military-political spending abroad onto the shoulders of other countries, and this naturally rouses vigorous resistance on the part of the latter and a growth of interimperialist rivalry.

Finally, the complete isolation of government agencies from money market activity, urged by Friedman, runs counter to the whole tenor of present-day state-monopoly capitalism, and is, for that reason, obviously utopian. When exchange rates were pegged, any change of parities was preceded by broad discussions in parliament and other public fora, but under floating exchange rates, intervention by central banks in the money markets becomes a routine daily practice not subject to any control by public forces. That is why as the world economic crisis advances, fluctuating exchange rates are fraught with danger of a "monetary war", i.e. a deliberate and headlong depreciation of capitalist currencies to obtain competitive advantages on world markets. But that is precisely what happened during the economic crisis of the 1930s. Such developments open up the prospect of a sharp aggravation of interimperialist contradictions and more economic and social upheavals in the capitalist world.

In recent years, the theory of floating exchange rates was largely realised in the practice of capitalist monetary relations. In March 1973, virtually all the leading capitalist currencies set out "on a float", although it was a "dirty" float, because of central-bank intervention in the money markets.

At the insistence of the United States, which has a stake in the floating exchange rates, for these enable it to use monetary dumping, a sharp instrument in the competitive struggle for marketing outlets and influence on the balance of payments, the Jamaica Agreement legalised this mechanism now and in the future. It is true that the new IMF Charter also contains a clause for a return to the system of stable (but more flexible) exchange parities. Up to now, however, most economists and financiers in the West have voiced highly pessimistic views about the possibility of a return to the system of pegged parities in the more or less immediate future.

At the same time, the facts show that the smoothly described and "elegant" academic model of floating rates, designed to solve all the contradictions of the international payments mechanism at a stroke of the pen, has been clearly skidding in the ditches of capitalist reality. One US expert on monetary matters, Charles A. Coombs, says that the results of free floating are disastrous: "In general, free or clean floating has been thoroughly discredited by its market place results."[1]

Let us note that even those bourgeois economists who are inclined to criticise the capitalist monetary and financial system do not go beyond pointing out some of its defects which have helped to produce the world monetary crisis, for their narrow class approach and the resultant gnosiological limitations prevent them from seeing the whole picture of the crisis and its underlying causes.

Accordingly, bourgeois economists as a rule say nothing about such key factors of economic and military-policy strategy of the imperialist powers as the vast external government spending which leads to monetary and financial upheavals

[1] Charles A. Coombs, "Some Thoughts on International Money". In: *The Banker*, London, December 1975, p. 1483.

in the capitalist world. They base their criticism of the Bretton Woods monetary mechanism, for instance, on superficial empirical observations, ignoring the fact that the monetary disorders are deeply rooted in the underlying antagonistic contradictions of the capitalist mode of production, the chief of which is the contradiction between social production and private capitalist appropriation. In international economic relations, this basic contradiction assumes the form of a contradiction between the objective need for greater internationalisation of economic ties and a deeper social division of labour, on the one hand, and the uneven and erratic development of world capitalism, on the other. Taken as a whole, this leads to a further sharpening of the competitive struggle between the capitalist countries.

In his *Capital*, Marx sarcastically called bourgeois economists "economic weather prophets" because they looked for the origin and cure of the violent storms in the world market "in the most superficial and abstract sphere of this process, the sphere of money circulation".[1] We find that not much has changed since then, and that explains why the recipes proposed by bourgeois economists for overcoming the monetary upheavals can do nothing to bring about real stabilisation of the monetary and financial mechanism of world capitalism.

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[1] Karl Marx, *Capital*, Vol. III, p. 547.

Part Two

CHAPTER SEVEN

INSTITUTIONALISM

This chapter deals with theoretical and ideological positions of the most prominent US institutionalists: T. Veblen, J. Commons, W. Mitchell, J. M. Clark, G. Means, G. Colm, J. Galbraith, R. Heilbroner, who have had a marked influence on 20th-century political economy and especially on the formation and development of bourgeois reformism.

This trend arose in US bourgeois political economy with capitalism's transition to its monopoly stage, when some bourgeois theorists were disenchanted with the doctrines advocating a free-competition market economy and could not accept the economic doctrine of liberalism with its principle of nonintervention of the state in the spontaneous course of development. That new line of thinking, to quote Robert Heilbroner, meant the emergence of "new ideas of social control" as a counterbalance to traditional liberalism.[1] Its champions took the objective tendencies towards greater "collectivism" as a point of departure and advocated the need to elaborate a theory of "manageable development".

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[1] Robert L. Heilbroner, *Between Capitalism and Socialism. Essays in Political Economics*, Vintage Books, New York, 1970, p. 10.

In their theoretical and ideological concepts, the institutionalists embodied the bourgeois-reformist notions on the historical evolution of capitalism and its transformation into a stable social system free of contradictions. These reformist notions were counterposed to Marx's concept of social development and the socialist revolutionary theory.

Having undergone considerable changes after its "historical peak" in the 1920s and 1930s, institutionalism was given a new lease of life in the mid-1960s. Thus, an Association for Evolutionary Economics was set up in 1965 to promote the institutionalist trend in economic science. Institutionalism came to exert a stronger influence on economic theory and state policy, on the social mentality and, above all, on the ideology of a sizeable section of the intelligentsia. As the contradictions in every sphere of social life were exacerbated and the earlier forms of state-monopoly regulation proved to be quite worthless, the methodological basis and the prevailing theoretical notions were revised and the Keynesian and neoclassical concepts of crisis-free and balanced development fell to the ground. There emerged a tendency to the "sociologisation" of economic thinking and economic doctrine, so that the ideas and methodological positions of the institutionalists came to attract greater notice, for they had always accentuated the role of social, political, socio-psychological, and ideological factors in economic processes and in the evolution of the social system as a whole.

At the same time, institutionalism has also been affected by the acute crisis of bourgeois economics. This crisis manifested itself in the repudiation of the discredited "ideology of industrial progress" and in the quest for a new methodological approach to economic analysis, in the recognition of the need to formulate a conception of social development that could provide a theoretical basis for purposeful state policy.

Discord and diversity of views within institutionalism itself is another manifestation of the crisis. Many new "intermediate" and "hybrid" concepts have emerged which comprise features of social-democratic reformism, petty-bourgeois utopian romanticism, and left-wing radicalism.

1. Methodological Specifics of Institutionalism

Institutionalism in US political economy was first brought to the fore in the late 19th and early 20th centuries by Thorstein Veblen, who is seen as its ideological founder.[1] In the 1920s and 1930s, the term "institutionalism" gained wide currency chiefly owing to the response evoked by Veblen's critical works. These became the "gospel" of the new movement in political economy, directed against traditional economic thinking and aiming to elaborate a comprehensive theory of social development.

One should point out, however, that institutionalism did not constitute a special school of thought in political economy with an acknowledged "leader" and a more or less integral theoretical conception, whose basic propositions would be shared and developed by the economists of this school. At every stage of its existence, institutionalism has been an amorphous and heterogeneous body of ideas. The various economists traditionally ranked among the institutionalists have differed widely in

[1] Thorstein Veblen (1857-1929) published 11 books, the major of which are: *The Theory of the Leisure Class*, Macmillan Co., New York, 1899; *The Theory of Business Enterprise*, The New American Library, New York, 1958; *The Place of Science in Modern Capitalism*, B. W. Huebsch, Inc., New York, 1919; *The Engineers and the Price System*, B. W. Huebsch, Inc., New York, 1921; *Absentee Ownership and Business Enterprise in Recent Times. The Case of America*, George Allen & Unwin, Ltd., London, 1924.

their theoretical and ideological positions, and also in the range of problems they have dealt with.[1]

What brings the institutionalists together is primarily their criticism of the orthodox neoclassical theory, its socio-philosophical and special methodological principles.[2] The institutionalists criticised the neoclassical conception of a competitive economy and its idea of a market equilibrium as a "normal" state of the economic system. They reviewed the neoclassical idea about some preordained harmony of economic interests, with any departures from that equilibrium being naturally and inevitably overcome.

In contrast to the neoclassical theory, which presents the market as a universal, neutral and highly efficient mechanism for distributing economic resources between their possible alternative uses, the new economists studied the market as a *social institution*, which is fundamentally transformed in the course of capitalism's evolution together with its whole institutional system.

The institutionalists criticised the neoclassical theory not so much by exposing the defects of its logic as by pointing to its narrow methodology, which ignored the role of social, political, and socio-psychological factors in the functioning of the

[1] In Soviet economic writings, institutionalism has been studied by I. G. Blyumin and L. B. Alter (see: I. G. Blyumin, *Essays in Modern Bourgeois Theoretical Economics. Social Trends*, Kommunisticheskaya Akademia Publishing House, Moscow, 1930; and *A Critique of Bourgeois Political Economy*, Volume 2, USSR Academy of Sciences Publishing House, Moscow, 1962; L. B. Alter, *Bourgeois Political Economy in the USA*, Moscow, 1971 — all in Russian).

[2] John Maurice Clark writes that the term "institutionalism" has been applied to a number of theories, some of them having "little in common except departure from 'marginalist' orthodoxy". (John Maurice Clark, *Economic Institutions and Human Welfare*, Alfred A. Knopf, New York, 1957, pp. 56-57.) Clarence E. Ayres expresses a similar idea in his *The Theory of Economic Progress. A Study of the Fundamentals of Economic Development and Cultural Change*, Schocken Books, New York, 1962, p. XI.

economic mechanism, and also by showing that its ostensibly neutral economic analysis in effect derives from a definite social philosophy with its own system of values.

From this angle, Veblen and the other institutionalists criticised the neoclassical marginalist doctrine of value and prices, the theory of the firm, and the doctrine of consumer demand.

Veblen had a strong influence on the subsequent development of institutionalist criticism of the neoclassical market doctrine, and also on research into the actually existing system of economic regulation, into the problems of monopoly and competition. In his first work, *The Theory of the Leisure Class* (1899)[1], Veblen gives a critical analysis of the system of social and everyday values in "commercialised" society. It is hardly surprising that interest in Veblen's book had a comeback more than half a century after its publication, when the evils of the US "consumer civilisation" were exacerbated to an extreme and when the question of the "criteria of values" appeared in a new light in connection with the "quality of life" problem.

The institutionalists centre their research on the market mechanism: the specific features of its functioning in the modern economy, its merits and fundamental defects, its potentialities and limitations. They contrast their methodology for studying market processes to that of the neoclassical school.

One should point out, however, that the institutionalists' criticism of the neoclassical theory is fairly limited. In arguing against the neoclassics, they are usually moved by an urge to supplement their economic theory in order to make it more "realistic" and, consequently, more effective. While criticising the basic methodological positions of the neoclassics in matters of value, prices and incomes, the institutionalists recognise the scientific validity

[1] T. Veblen, *The Theory of the Leisure Class.*

of neoclassical theory in an economy where the market is the sole and all-embracing regulation mechanism.

Criticism of the market mechanism lies at the root of the institutionalist doctrine on the contradictions between private and social interests under capitalism and on the possibility of coping with these contradictions through state regulation. Institutionalist concepts present such regulation as a vital need, as purposeful and systematic activity on the part of the state to perform functions which the market mechanism is in principle unable to perform, and also as an effect to stabilise, correct and regulate the market mechanism itself. The institutionalists advocate a system of social control over the economy which would help to make effective use of all the potentials of the market mechanism, remove its negative features and compensate for its shortcomings.

The institutionalists maintain that one of the basic "defects" of the market mechanism is that in a market economy, the social costs of production cannot be fully reflected and calculated. The market process registers in money terms the private costs of production, but the damage done to the environment and the "social costs" of private capitalist enterprise are not reflected in market evaluations.[1]

According to present-day institutionalists, another limitation of the market mechanism is that it takes into account and ensures the satisfaction only of those social requirements which are represented by effective demand, while requirements in education, health care, and other social benefits should be satisfied at the expense of taxes. These requirement spheres are neglected and lag far behind, since in a market economy there is no

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[1] See: J. M. Clark, *Preface to Social Economics*, Tarrar & Rinehart, Inc., New York, 1936; and *Social Control of Business*, The University of Chicago Press, Chicago-Illinois, 1926.

mechanism for meeting these requirements equivalent to the one which stimulates outlays on the market production and consumption of goods and services. Meanwhile, socio-cultural services tend to acquire increasing importance for economic progress and for social well-being in the broad sense of the term. The gap between the development level of marketable goods and services, and services meant for non-market collective consumption is becoming one of the most glaring contradictions of present-day capitalist society.

The institutionalists devote much attention to the "deformation" of the market mechanism owing to the sway of the monopolies and to private-monopoly regulation of prices and production; to the contradictions deriving from the two-tier structure of the modern economy: the relationship between the giant corporations and small and medium-scale enterprise.

The institutionalists maintain that in a highly developed economy, where giant monopolies play the decisive role in production and where there have been considerable changes in the level and structure of mass consumption, market instruments of economic regulation are bound to play a lesser role. At this stage of development, the behaviour of economic subjects (producers and consumers, buyers and sellers) can no longer be determined solely by market incentives and impulses in every given period of time. Extra-market and extra-economic factors and considerations come to play an ever more important role in the economic process, and economic decisions are taken with a view to the longer term.[1]

The institutionalists seek to study the interplay of economic and non-economic factors in socio-

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[1] See: Robert L. Heilbroner, *The Future as History,* Harper & Row Publishers, New York, Evanston, London, 1965; also his: *The Economic Problem,* Prentice-Hall Inc., Englewood Cliffs, New Jersey, 1970.

economic development, the structural, organisational, and functional aspects of the economic mechanism as a whole, regarding the economic sphere as part of an integral social organism interacting with the various other subsystems. Economic theory here comes into close contact with other social disciplines (sociology, political science, social psychology, and so forth), and the aim is to overcome their self-sufficiency and isolation from each other.

In this line of thought, institutions are the main object of research: their origins, evolution, and role in determining the economic behaviour of individuals and social groups, and state policy.

The concept "institution" is taken in the broadest sense of the word, covering economic organisation (forms of property, management-organisation structures, modes of interaction, etc.); the organisation of political affairs and state power; the judicial system and the interrelationships among the various social groups; conventional social usages and national traditions; the peculiarities of the mass consciousness and the structure of ideological values.

Although the institutional system is considered in a concrete historical setting, the institutionalists see it as a product of law-governed, spontaneous evolution and an object of conscious influence through reformist efforts. Research into the evolution of the institutional system engendered the institutionalist concept of stages of social growth, and the attempts to bring out the national specifics of the "institutional environment" in different countries stimulated the comparative analysis of economic systems as a section of economic science.

In contrast to closed, deductive economic concepts, the institutionalists came up with an "interdisciplinary" approach to economic analysis in a concrete socio-historical context; and in contrast to "pure analysis", they advocated a comprehensive study of the actually existing economic system. Disagreeing with the neoclassics' extra-historical abstract theoretical constructs, the institutionalists tried to use the historical method of research: to consider real phenomena in their dynamics, bringing out causal connections, the factors determining the course of development, its motive forces and prospects.

The US philosophers Charles Peirce and John Dewey, the founders of pragmatism and instrumentalism, who formulated a "practical" concept of truth, an "anti-doctrinaire" principle of relativism in the theoretical field, and the idea of active influence on social conditions, plaved an important role in laying the philosophical groundwork of institutionalism.

Institutionalism was also influenced by the German "historical school", with its empiricist, anti-deductive approach, its concept of society's stadial development, and its accentuation of the role of juridical norms and state policy in social development. There is also deep ideological kinship between the institutionalists and British sociologists and economists advocating bourgeois reformism, among whom John Hobson plays the most prominent role.

The institutionalists combine a critical and "negative" approach with a "positive" urge to elaborate the problems being considered with pragmatic aims and views, in order to reform and modernise the existing system. Individual economists combine these two principles in various ways, giving preference either to the one or to the other. As John M. Clark put it, Veblen and Commons represent the "two poles". Veblen levelled incisive sarcastic criticism at the business civilisation. He renounced that civilisation ideologically, did not offer any political recommendations, and on the whole took a "pessimistic" view of the prospects of the capitalist economy. In contrast to Veblen, Commons' approach was an epitomy of pragmatism.

In criticising the neoclassical concept of the market mechanism and Edward Chamberlin's doctrine of monopoly competition, Clark himself came up with a "positive" elaboration of the problem of costs under large-scale production, the dynamic theory of competition, and the economic cycle theory, winning recognition in academic and business circles. Clark's concepts of "socio-liberal planning" and social welfare were aimed to preserve capitalism by improving it.

Wesley Mitchell also sought to study economic processes with "positive" aims in view. In his "optimistic belief" that national planning could help to overcome the vices of capitalism, Mitchell concentrated on the economic cycle, seeking to introduce into economic science the principle of "empirical realism" and complex "interdisciplinary" economic analysis so as to ensure social stability and to make the cycle milder.

Owing to their reformist attitudes and their striving for a complex and dynamic analysis of the economic system, the institutionalists pioneered research into many new phenomena and gave a new reading to various problems within the framework of bourgeois political economy. They studied the concentration of production and capital, the mechanism of property and control, the economic power of monopoly corporations, conflicts among various economic interests, the relationship between the private and the state sector, and state regulation.

A characteristic point to note is that many of these problems, which are now being studied by neoclassical or Keynesian theorists and fall within the compass of their research, were first formulated in bourgeois political economy by institutionalist economists. Their initial propositions, which were first formulated by way of criticism and were seen by the orthodox majority as heterodoxy or downright heresy, were gradually accepted.[1] In the

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[1] Thus, John Hobson's idea on surplus savings was widely recognised in the 1930s in view of the worst ever world crisis. J. M. Clark wrote in an article on Hobson's contribu-

mid-1960s, various problems first raised by the institutionalists in US bourgeois economics (like those of "social overhead costs", negative extra-market effects of production and consumption, and "the costs of economic growth") came to the fore as crucial problems calling for theoretical analysis.

Institutionalism has not created any "constructive", theoretically integral conception that could help to govern socio-economic processes. Such a theory, the institutionalists believe, should be developed by "restructuring" the existing economic theory into genuine "political economics". Such a theory, they say, should be eclectic: it should assimilate the valuable ingredients of all other doctrines. Many present-day institutionalists hope that it may be possible to produce a realistic and effective economic theory by "synthesising" the traditional neoclassical and the institutional approach, and others (like Robert L. Heilbroner) that political economics should be produced by "marrying" Marxian insights to neoclassical techniques.[1]

One of the major methodological works put out by the institutionalists over the past few years is Adolph Lowe's book, *On Economic Knowledge. Toward a Science of Political Economics.*[2]

Lowe's idea is that "political economics" should service the administration of the economy in order to obtain definite goals. These goals should be formulated to ensure that when they are attained the economy would meet the normative criteria

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tion to economics that "serious investigation of this former heresy has become unqualifiedly respectable". (J. M. Clark, "John A. Hobson: Heretic and Pioneer (1858-1940)". In: *Journal of Social Philosophy*, New York, July 1940, Vol. 5, No. 4, p. 356.

[1] Robert L. Heilbroner, *Between Capitalism and Socialism*, pp. 124, 125.

[2] Adolph Lowe, *On Economic Knowledge. Toward a Science of Political Economics*. Harper and Row Publishers, New York and Evanston, 1965.

of "satisfactory" functioning (in the use of resources, the volume and structure of production, income distribution, and so on). The economic theory should enable its advocates both to formulate goals, and to choose the methods and instruments for influencing the behaviour of economic subjects, so as to ensure the efficient functioning of the entire economy. On the whole, the institutionalists advocate a normative approach to the development of economic problems, saying that evaluations have to be scientifically validated in order to "fuse" science and ethics.

Since the institutionalists are critically-minded and aim to study the motive forces of economic development and the tendencies in the evolution of the capitalist system, many of them are interested in Marxism. They often say that Marxism is one of the theories lying at the origin of institutionalism. What they particularly appreciate about Marxism, they say, is its method: the historical approach, the dynamic nature of the theory, and the "integration" of the economic and sociological aspects, of microeconomic and macroeconomic analysis.

Nevertheless, all institutionalists, whatever their leaning, have always contrasted their theory with Marxism. They do not see capitalism as an exploitive system with a fundamental contradiction between the social nature of production and the private capitalist mode of appropriation, with its basic class antagonism between labour and capital. They counter the Marxist theory of historical progress through class struggle with their own concept of "social solidarity".

The ideological and methodological positions of the institutionalists manifest themselves most clearly in their reading of capitalist contradictions. They believe that the deepening crisis of the present "industrial civilisation" is due to the discrepancy between the pace of progress and development levels of the scientific and technical sphere and industrial technology, on the one hand, and the institutional system, on the other. They maintain that if this discrepancy is to be overcome, it should be socially recognised and a new and universally accepted system of social and ethical values should be formed to meet the new conditions and society's requirements at the present stage of its development. On this basis, new "codes of behaviour" should be developed for various social groups in order to unite all the social forces and rally them to the solution of imperative problems.

This scheme of social progress is based on a peculiar methodology, when the system of social production is divided into "production" as such, which develops in accordance with the logic of universal "imperatives of industrialism", and "institutions" as embodying the social mode of production in its concrete historical and national forms. Science and technology lying at the root of "production" are seen as the leading factors behind the historical changes at the present stage of industrial development: these constructive dynamic forces necessitate and make inevitable the subsequent "adaptational restructuring" of the institutional system.

True, in the 20th century, the importance of applied scientific knowledge has vastly increased. Nevertheless, even today scientific and technical progress is not a self-sufficing force "purged" of any social elements and operating outside the institutional framework. It exists in definite social forms, and, what is particularly important here, the nature and limitations of "adaptational" institutional changes are determined, in our opinion, by the socio-political conditions. While creating definite prerequisites and necessitating social change, scientific and technical progress does not determine the pace and mechanism of such change. The "dichotomy" of scientific knowledge into industrial technology, on the one hand, and institutions, on the other, is a characteristic principle of institutional methodology. It is particularly pronounced in Veblen's works, where one can locate the origins of the industrialist-technocratic concepts shared by many present-day institutionalists. Thus, Veblen saw the basic economic contradiction of 20th-century capitalism as that between "industry" and "business", which geared production to its own financial interests. According to Veblen, "industry" as such (the whole sphere of material production or the sphere of functioning of real capital) does not contain any social antagonisms. He associated capitalist society's contradictions and conflicts chiefly with the functioning of capital in the financial sphere and with fictitious capital, with their pressure on "industry".[1] The institutionalists reject the concept of surplus value and exploitation as a social-class category expressing the substance of relations between antagonistic classes. They profess an "extra-class" stand in defence of social interests.

Veblen gave a "dichotomic" reading of the real processes separating capital as a function from capital as property, separating property from direct managerial functions. He showed the real power of property, which is connected with a definite system motivating the economic behaviour of large companies, their goals, and the choice of means for achieving these goals. At the same time, Veblen potrayed property under the corporate system as something external to production.

Veblen believed that society's collective interests coincided with those of unimpeded growth of production efficiency. That is why he saw engineers and other specialists working in industry as direct and natural vehicles of social interests, regarding them as a homogeneous class, whose class consciousness manifested itself in an intolerance of waste, of a limited use of the potentialities of modern

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[1] T. Veblen, *The Theory of the Leisure Class*; also his: *The Theory of Business Enterprise.*

technology or their misuse.[1] Engineers personify the scientific approach, sensing the need for "rationality", dictated by the nature of modern production technology.

The theory of the "dichotomy" of industry and business reflected definite technocratic illusions and, to some extent, helped to sustain these. Veblen's conflict between the interests of "industry" and "business" has variously affected the works of Commons, Mitchell, Tugwell, Means, Ayres, Galbraith, and Heilbroner, determining their views on the "basic" contradiction of present-day capitalism.

R. Tugwell presents this conflict as a discrepancy between the "logic of the economic system" (which he sees as extra-social) and business ideology, which is out of touch with the objective conditions and requirements of economic development in the 20th century.

Commons also gives a dichotomic reading of the activity of big corporations. As he sees it, the corporation has two opposite aspects. One of these covers matters relating to the optimal organisation of production meant to satisfy social requirements. As such, production is seen as socially sterile, and the corporation, as an outfit whose purpose is to achieve maximum economic efficiency. The second aspect of its activity relates to its functioning as an organisation of Big Business, whose purpose is to achieve utmost efficiency in the accumulation of money values, to maximise its profits and the value of its assets.

Commons distinguished two types of economic power (and two types of profit-making), one of which derived from production efficiency, and the other, from the possibility of putting pressure in the sphere of market relations. The latter type of economic power, Commons believed, should be the

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[1] T. Veblen, *The Engineers and the Price System.*

prime object of state regulation. According to Commons, one of the main lines in "rationalising" capitalism is to create conditions under which the market positions of the various companies and their ability to make profit would correspond to their contribution to the national income, to the efficiency of social production; in other words, the aim is to rule out the possibility of obtaining "unearned" income ("unjustified" from the standpoint of society's interests) through overpricing, exploitation of consumers and manipulation of output.

The works of John Kenneth Galbraith, the most popular present-day institutionalist, epitomise the contradictory stand of the institutionalists as bourgeois critics of the capitalist system, the general philosophical principles and the concrete methodology of that criticism.

Galbraith deduces the principles of viability and the behaviour of the large firms from the specifics of modern "technology", from the needs of large organisations as such. He defines technology as a systematic application of scientific and other knowledge in an organised form to the solution of practical problems. "Technology" is seen as an "imperative", an objective factor, with its own logic of motion, which can through corporate planning revolutionise the operation of the whole economic system.

According to Galbraith, the "technostructure" is the vehicle of the interests of large corporations.[1]

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[1] John Kenneth Galbraith, *The New Industrial State*, Houghton Mifflin Co., Boston, 1967; Galbraith's concept of "technostructure" is indistinct not only in social, but also in structural terms, including corporate managers of every rank, lawyers, engineers, economists, auditors, advertisers, and sales managers. The concept of "technostructure" and "the mature corporation" has been criticised by some economists from the New York based New School for Social Research. (See: Robert L. Heilbroner, "Capitalism without Tears". In: *The New York Review of Books*, June 29, 1967; Edward Neil,

With definite reservations, one can accept this. The whole point, however, is that these interests themselves (the way corporate goals are formulated and attained) reflect the substance of a socially definite type of organisation, rather than some techno-economic "imperatives" as such or the "extra-social" aspirations of the technostructure for rationality.

Galbraith contrasts the power of the "technostructure" in "mature corporations", which manifests itself in corporate planning, with the power of the market, regarding these as two ostensibly incompatible principles of economic organisation. As he said in his *The New Industrial State*, it helps to dovetail the economic interests of the large firms with those of society as a whole. It is hardly surprising, therefore, that he draws a direct analogy between planning under the "new industrial system" and planning in the socialist countries, confusing two essentially different types of organisation of social production: the planned economy, where the system of centralised planning is based on socialist property and serves the interests of social production, and the capitalist economy, where private-monopoly planning and state regulation interact with competition. Galbraith has in effect overlooked the problem of the socio-economic basis of social production, concentrating on the management of large firms by career managers.

In his book, *Economics and the Public Purpose*, Galbraith describes two types of contradictions in the US economy: first, those between the interests of the "planning system" and society; and second, those between the "planning" and the "market" systems. Both are seen outside the context of the exploitive system, and are presented as engendered by the sway of purely economic goals geared to pave

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"Economics: The Revival of Political Economy". In: *Ideology in Social Science. Readings in Critical Social Theory*, Ed. by R. Blackburn, Fontana/Collins, 1972.

the way for unimpeded economic growth within the framework of the "planning system", as a manifestation of the discrepancy between economic thinking, doctrine and policy and the actual conditions and requirements of social development.

Thus, Galbraith maintains that the basic interest of the big corporations—ensuring sustained growth—is incompatible with exploitation of consumers through the mechanism of monopoly prices, and so denies that the large firms are monopolies. Simultaneously, he draws the conclusion that exploitation of workers is not typical of the "planning system".

In full accordance with the traditions of bourgeois political economy, Galbraith uses the "market" concept of exploitation. With respect to the consumer, he associates exploitation with overpricing (as compared with the "normal" competitive level), and with respect to the workers, he associates it with underpayment for their labour. If an employer in some industry can dictate his own terms, so that the workers get less than they would have been entitled to under free market competition, it means that they are being exploited. According to Galbraith, the "planning system" reduces exploitation in this "precise sense of the word" to a minimum. He says that exploitation is widely practised only under a "market system" and in the sphere of interrelations between the "planning" and the "market" system both on a national scale and on the scale of the whole world, where the industrially developed capitalist countries represent the "planning system" in contrast to the market economy of the developing countries.

In considering the relations between capital and labour, the institutionalists invariably restrict these to the "industrial sphere", substituting questions of "rivalry" between the corporations and the trade unions over the terms of employment and payment for the problem of the antagonism between the class interests of the bourgeoisie and the workers.

The institutionalists characteristically claim that they take an "extra-ideological" stand, and that their recipes for reforming the existing institutions express the interests of society as a whole and, consequently, the scientifically cognised requirements of its development. The contradictions between different social interests are presented as contradictions or mistakes in doctrine, policy and ideology, which can and should be overcome through the development of the social consciousness, the elaboration of an up-to-date theory, and improvement of the state regulation mechanism. This approach helps to obscure the social nature of the capitalist system's contradictions and its class antagonisms.

2. The Contradictions of Capitalism and the Problem of Social Control over the Economy

The bourgeois-reformist conceptions of social control over the economy in present-day capitalist society have developed along two lines. The first and earlier line advocates reform of the major companies and state regulation of the market mechanism of competition. The second line advocates the need to set up and develop a state system of indicative planning. These two lines are distinct but closely tied in with each other.

The institutionalists start from the premise that at the present stage of concentration of production and economic integration, the competition mechanism has lost its role of universal, freely operating regulator.

They reject the orthodox premise that the 20th-century economy is competitive both in structure and functioning. Within the framework of institutionalism, there has emerged a broad and heterogeneous trend dealing with the problems of monopolisation and the specifics of the market mechanism under private-monopoly regulation of prices, volume of production, and investments. This trend is represented by G. Means, Clair Wilcox, Corwin Edwards, W. H. Hamilton, Marshall Dimock, Joel B. Dirlam, R. Brady, George W. Stocking, Myron Watkins, Theodore Kreps, and John M. Blair.

In elaborating the problem of monopolisation and private-monopoly regulation, the institutionalists consider matters relating to the concentration and centralisation of production and capital at the level of enterprises, companies, industries, and the national and global economy. In the early 1930s, G. Means was the first US economist to present aggregate indicators showing the concentration of economic power in the hands of the major corporations and to formulate on that basis the theory of "administered" prices and markets.

The institutionalists now centred special attention on the functioning corporation as an "institution", dealing with questions like the "disintegration" of property and management, the role of career managers, and the behaviour motives and purposes of the big corporation, the lowest tier in the economic system of present-day corporate capitalism. In contrast to neoclassical theory, they developed their own theory of the firm.

The institutionalist recipes for reform envisage the formation of an efficiently operating "mixed economy": a combination of private and public sectors, development of state controls over the activity of big corporations and market regulation methods, and the formation of a new mechanism for public control over the economy, which would make it possible to exert a purposeful influence on the course of development. The hopes pinned by the institutionalists on government regulation did not come true. Moreover, the actual course of events showed that the objects of regulation could subordinate the activity of the regulating bodies to their own interests and turn these into an effective instrument for maintaining and multiplying their economic and political power. The regulating bodies were made to serve Big Business, making it easier for the latter to establish and maintain group monopoly in the regulated sectors.

Since the results of such regulation were disappointing, institutionalist concepts gradually evolved from the idea of supervision over the big companies to the idea that it should be fitted into a system of national and regional planning for guiding the development of the corresponding industries and government influence on the formation of the volume and structure of the final consumer demand for services in the given sphere. Present-day institutionalists who specialise in the theory and practice of public utility regulation maintain that the use of plan guidelines coupled with economic and juridical incentives and restraints in a new system of accounting and control would put the corporations within definite bounds, confining managerial activity to a drive for efficiency.[1]

Ever since the turn of the century, the institutionalists have mooted the idea of socialising the large companies through government supervision over their activity. At the present higher stage of private-monopoly socialisation, Big Business has again come under criticism. The problem of public control over the activity of large corporations has become most acute. There is no unanimity among those who want the corporation to be reformed as a public institution. Some advocate a special federal status for the major corporations (an idea formulated back in the 1930s by the institutionalists), which would limit their prerogatives and

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[1] Harry M. Trebing, "Realism and Relevance in Public Utility Regulation". In: *Journal of Economic Issues*, Vol. VIII, No. 2, June 1974, pp. 209-233.

gear their activity to public interests. Others emphasise the need to develop a mixed, private-and-state form of organising production.

Thus, Means suggests the adoption of a special act which would pledge the big corporations to abide by definite rules in accordance with the "economic logic of the collective enterprise". He also urges the need to introduce a standard and sophisticated system of accounting, reporting and supervision over the activity of the big corporations; to reduce the rate of profit on after-tax capital by about 10 per cent; and to elaborate a system for evaluating the performance of the top managers and a corresponding system of inducements for the efficient running of corporations (rewards for lowering costs and improving other indicators). While offering the recipe of reducing monopoly profits to "normal", Means does not call in question the very principle of private property in capital and the "legitimacy" of dividends as a form of realising the right in property.[1]

All such reasoning starts from the premise that there has been a "corporate revolution" in the course of which the owners of capital have been separated from the management. Management here is identified with the administrative function, that is, with the right directly to adopt and carry out decisions. The concept of "collective enterprises" and the scheme for institutional reform based on that concept ignore the power of finance capital and, in effect, the role of large-scale capitalist property as an "institution".

One can hardly object to the idea that monopoly profit should be limited or to the proposition that state control over price levels and movements calls for the use of definite price guidelines and normative criteria for profit rates. But the advocates

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[1] Gardiner C. Means, *The Corporate Revolution in America*, The Crowell-Collier Press, New York, 1962.

of these reforms say nothing about the most essential question: about the practical ways to ensure government control over the use of resources and cost formation.

The "strategy of reform" formulated by J. K. Galbraith in his *Economics and the Public Purpose* is another model for "socialising" the big firm.

As the main reform in the "planning system", Galbraith advocates the need to socialise the corporations belonging to the military-industrial complex (those which produce more than half their output under government contracts). Such corporations should be converted into public corporations through purchase of shares from the shareholders. The other big corporations would be gradually converted into "fully public corporations" or "socialised" through public purchase of the stock with fixed interest-bearing securities. In time, Galbraith believes, private wealth would be gradually and naturally dispersed and cease to exist owing to inheritance, taxes, philanthropy, and inflation.

So, Galbraith sees the problem of eliminating big capitalist property and replacing it with public property—the fundamental economic problem of social revolution—as an organisational-technical aspect of the policy of reform. He maintains that the "fully mature corporations" have completed the "euthanasia of stockholder power", which has given way to the "technostructure". In his opinion, there could hardly be much resistance to such reform, for there would be no point in protecting "capitalist interests proper" since the stockholders would be compensated and would not suffer, while the corporate technostructure would simply operate in accordance with the demands enacted into law by the legitimate government authorities.

In institutionalist concepts, property never plays the decisive role. It is seen as a system of rights enacted in legislation rather than as a system of social production relations.

In his "strategy of reform", Galbraith assigns the key role to changes in government economic policy. This policy, he says, should and can be aimed at rechannelling the activity of large firms to serve the public interest. For this purpose it is necessary to limit the influx of resources into overdeveloped industries; to change the system of priorities in government expenditure; to regulate or prevent the development of socially damaging lines of production and consumption (environmentally, etc.) or which in any other way go against the public interest. He says that the state should intensify its anti-cyclical policy and do more to coordinate and balance the "planning system", and to exert a purposeful influence on the investment process and income distribution.

Reformist concepts for stabilising and "democratising" capitalism devote much attention to government policy with respect to small and medium-scale enterprise. Thus, in his "strategy of reform", Galbraith attributes paramount importance to measures meant to promote the development of the "market system", to increase incomes within that system and make these more reliable, and to strengthen its positions vis-a-vis the "planning system".

One peculiar feature of the reforms suggested by Galbraith is that he presents these as a "new theory of socialism", called into being by the specifics of the modern economy and meeting its requirements. The key chapter of his book on the strategy of reform is meaningfully called "The Socialist Imperative". In emphasising that his "new socialism" is objectively conditioned, Galbraith explains that it is not a matter of ideological preferences or the traditional problem of political choice between capitalism and socialism, but of developing the existing "elements of socialism", without which US society would not be viable.

Since Galbraith regards the inequality between the "planning" and the "market" systems and the gap in their development levels as the central structural problem of the modern capitalist economy, he maintains that the need for socialist transformations is primarily engendered by "the lag in the development of the market system". The way to harmonise planning and market, he believes, is to reform the "market system" and dovetail it with a modified "planning system". A part of the "market system", he says, has to be "fully socialised": housing, city transport, health services and other sectors that are of particular importance to society. For the rest of the market system he suggests cooperation, steps to set up trade and production associations.

In casting about for ways to harmonise private and public interests through reform from above, the institutionalists have always hoped that Big Business will "reform itself", believing that the monopoly corporations are capable of "self-socialisation". This term implies changes in the behaviour of the big corporations which would make it possible to some extent to coordinate their activity and overcome the "excesses" of monopoly competition; to accord the interests of capital owners with the interests of factory and office workers and the interests of the consumers; and to involve the corporations in the solution of national problems (protection of the environment, complex development of education and occupational training).

In the United States, which has the world's biggest monopolies, the traditions and ideology of "free enterprise" are stronger than in other capitalist countries. Hence the numerous theories on the "self-socialisation" of Big Business ("corporate socialism", "social responsibility" of managers, "the mature corporation" as a new social institution, a "new code of ethics" for big companies, etc). The ideologists of the monopoly bourgeoisie have been actively using these theories to counter the ideas on the need for government regulation of the economy, control over the big corporations, and development of social legislation.

In the past few years, some prominent spokesmen of monopoly business have also been urging the corporations to "reform" themselves and enhance their "social responsibility". The democratic movement, with its demands for protection of the environment, its efforts to uphold consumer interest, and its stand against artificial scarcities and price inflation, poses an ever greater danger for Big Business. In these conditions, the more "far-sighted" section of the monopoly bourgeoisie resorts to preventive measures, giving up some of its privileges and profits in order to retain its basic positions.

The second line along which the institutionalists have sought to reform capitalism is that of national indicative planning. The formation and evolution of planning concepts reflect the response of some bourgeois theorists to the contradictions of monopoly capitalism, on the one hand, and to the theory and practice of planning in the Soviet Union and other socialist countries, on the other.

Since the institutionalists have no integral politico-economic theory of indicative planning, their debates on this matter are largely confined to the pragmatic plane. Ever since the 1920s, they have been looking for a "middle way" between the two extremes; centralised directive planning ("full collectivism") and the policy of *laissez-faire*.

The main hopes here were pinned on "experimentalism" in the sphere of relations between private enterprise and the state. Recalling the 1930s, when the United States was the scene of spirited sociophilosophical debates on planning, and speeches by the advocates of the "new progressive approach" echoed widely across the country, the US historian of economic thinking Lewis H. Haney remarks that while seeking to play a positive part in solving the problem of social control over the economy, the institutionalists (W. H. Hamilton, R. G. Tugwell,

G. C. Means and W. E. Atkins) openly admitted that they had no clear idea of the purposes and methods of such control, professing "a sort of planless planning".[1] While aspiring to a thorough review of neoclassical economic theory and liberalist social philosophy, the institutionalists have been unable to counter these with a new and well-substantiated theoretical platform and political line.

Some economists believe that planning is one of the instruments of state power and should be used to enhance the "social justice" and stability of the existing economic system. Others see it as a new and much higher stage in centralised economic control, when private business is "straitjacketed" to discipline its activity, and when the state exerts a balanced influence on the investment process and incomes distribution and ensures the allround development of the public services. The idea of national planning, whatever its version, always implies a search for "hybrid forms" of social economic organisation. Reformist theorists hope that indicative planning will not only flatten out the economic cycle, but will also help to stabilise the capitalist system over the long term.

The idea of social compromise and the principle of free will and social cooperation are a specific feature of the bourgeois-reformist concepts of planning. The reformists hope for the development of a "sense of common interest", "social responsibility", "the cooperative spirit" and corresponding norms in the behaviour of social groups and economic agents, emphasising that production should still be run by private business. The state should only ensure reliable information facilities for the latter and use mostly indirect measures to control and influence it through monetary, credit and fiscal

[1] Lewis H. Haney, *History of Economic Thought*, The Macmillan Co., New York, 1949, pp. 720-721.

policies. In the United States, such a concept of "socio-liberal planning" was elaborated by W. C. Mitchell, J. M. Clark, G. C. Means and G. Colm.

Mitchell sees planning as a permanent adaptation process aimed to prevent imbalances and disproportions, to stabilise socio-economic development, to tone down contradictions and prevent these from exploding. Mitchell stressed that planning should not be used as an emergency measure only in exceptional circumstances (wartime, crisis slump, etc.), but should be permanent. He said that planning would make progress with the development of science and the information service, methods of influencing men's minds, the spread of an "ethic of mutual understanding" and "socially responsible" behaviour of social groups with different interests.

J. M. Clark was one of the first bourgeois political economists to take note of the discrepancy between private and public costs. He thought the gap could be narrowed with the help of measures designed, first, to even out market fluctuations in economic activity, which lead to under or overexploitation of economic resources; and second, to reduce the negative "external effects" (for the social and natural environments) of private-capitalist enterprise.

Means advocated planning based on an evaluation of the essential production resources and essential requirements on a countrywide scale. This, he said, should primarily apply to the allocation of new investments in a minimum number of key industries. With respect to private enterprise, planning should be indicative. Its purpose is to provide the necessary information and offer general guidelines for the adoption of particular decisions, and also for the government's fiscal and monetary policy.

After the war, Colm became one of the more prominent exponents of indicative planning. Planning was necessary, he believed, because investments and consumption in the private sector, and also the development of private and public sectors could not be balanced out automatically.

In the 1970s, when crisis processes marked by inflation and mass unemployment developed in the United States, the institutionalists somewhat modified their views on planning, urging the need to gear economic growth to the long-term interests of social development, and to assess that development on the basis of a broad complex of criteria reflecting the "quality of life".[1]

Thus, in *An Inquiry into the Human Prospect*, Robert L. Heilbroner admits that "the values of an industrial civilisation, which has for two centuries given us not only material advance but also a sense of *élan* and purpose, now seem to be losing their self-evident justification", giving way to "doubts and disillusions".[2] If economic development is to be directed in the interests of society, he says, there will have to be a "full-fledged transformation of 'private' capitalism into planned 'state' capitalism".[3]

In emphasising the need for a qualitatively new level of the state's purposeful influence on economic development, many institutionalists have come out in favour of state control over the formation of prices (primarily on the products of big corporations) and incomes (wage rates, established through the mechanism of collective bargaining, and profits). Special attention here is devoted to the need for an egalitarian state policy of redistributing incomes. The institutionalists see these reforms as a way of bolstering up the main capitalist institutions,[4]

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[1] Allan G. Gruchy, "Government Intervention and the Social Control of Business; The Neoinstitutionalist Position". In: *Journal of Economic Issues*, Vol. VIII, No. 2, June 1974, pp. 235-249.

[2] Robert L. Heilbroner, *An Inquiry into the Human Prospect*, W. W. Norton & Co., Inc., New York, 1974, p. 21.

[3] *Ibid.*, pp. 57-58, 84.

[4] *Is Economics Relevant? A Reader in Political Economics*, Ed. by Robert L. Heilbroner and Arthur M. Ford, Goodyeur Publishing Company, Inc., California, 1971.

as a way to conserve capitalism "that will improve its performance, enhance its reputation, increase its capacity to survive".[1]

3. The Institutionalist Concept of Transforming Capitalism

The institutionalists regard society's contradictions as separate unresolved problems or groups of problems without any common roots. Capitalist society's contradictions are seen as manifestations of the uneven development of the various aspects and components of the techno-economic, social and political mechanism. They see "institutional lags" as the key to social development.

The institutionalists devote much attention to the "adaptational mechanism", analysing the prerequisites and the ways and means to overcome structural, organisational, ideological, and other "institutional lags", and the mechanism for adapting the system as a whole and its various elements to new conditions and requirements. The institutionalists see the "adaptational mechanism" as an interplay of the factors and forces developing "from below" (i.e. from within the economic system itself) with the factors and forces introduced "from above", through reform, legislation and government economic policy.

Institutionalist economists differ widely on matters like the scale, methods and concrete content of reform, but institutionalist thinking as a whole has some general features. All advocates of the reformist concept of "administered evolution" believe, as it was pointed out above, in the possibility of cooperation between social classes and groups and in the emergence of a "new ethics of behaviour"

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[1] John Kenneth Galbraith, *Money: Whence It Came, Where It Went*, Houghton Mifflin Co., Boston, 1975, p. 312.

reflecting the development of a "collectivist" social mentality. J. M. Clark, who came out in the postwar period with several socio-philosophical works, emphatically argued that it was possible to save the capitalist system from "full collectivism" (that is, from political revolution and restructuring of society on socialist lines), on the one hand, and to avert the threat of fascism, on the other, only by developing and realising the principle of a "voluntary social contract" and recognising the need for conscious action to "rationalise" the system and harmonise different interests.[1]

The concept of social solidarity was most fully spelt out by the US institutionalist J. R. Commons, especially in his book, *The Economics of Collective Action.*[2] In contrast to the Marxist theory of class struggle, Commons formulated the concept of "industrial evolution", which boils down to the idea that social conflicts should be used as an effective instrument of economic progress.

Commons was the ideologist and practitioner of the movement for reform in industrial and social legislation and had many followers.[3] As the US economist K. E. Boulding put it, "Commons was the intellectual origin of the New Deal, of labour legislation, of social security, of the whole movement in this country towards a welfare state".[4]

[1] John M. Clark, *Alternative to Serfdom*, Alfred A. Knopf, New York, 1948; also his: *Guideposts in Time of Change*, Harper and Brothers, New York, 1949.

[2] John R. Commons, *The Economics of Collective Action*, The Macmillan Co., New York, 1951; also his, *Institutional Economics. Its Place in Political Economy*, The Macmillan Co., New York, 1934; and *Legal Foundations of Capitalism*, The University of Wisconsin Press, Madison, 1957.

[3] Kenneth H. Parsons, "The Basis of Commons' Progressive Approach to Public Policy". In: *Labour, Management, and Social Policy. Essays in the John R. Commons' Tradition*, Ed. by Gerald G. Somers, The University of Wisconsin Press, Madison, 1963.

[4] Kenneth E. Boulding, "A New Look at Institutionalism". In: *The American Economic Review*, Vol. 47, No. 2, May 1957, p. 7.

Commons believed that the way to create a "rationally organised" capitalist society was to improve and develop the institutional machinery for achieving voluntary and compromise agreements to harmonise clashing interests. What he meant was not only conflicts in industry, but all other social conflicts as well.

The theory of "social conflict" as an antithesis to the theory of class struggle could be presented as follows: social conflicts are not antagonistic and are not underpinned by class, production relations. Conflicts are manifestations of various aspects of the interplay of different social groups in one social organism; they are a necessary and inevitable stimulating factor of social evolution, of social progress; conflicts should be resolved through "institutionalisation" (that is, through "rational settlement") on the basis of definite procedural rules, establishment of appropriate arbitration bodies, and use of legislative and political measures.

According to Commons, the key purpose of "scientific management" in industry is to ensure mutual understanding and cooperation between the employers and the employed. Mutual "good will" is seen here as an ever more important element of the "intangible assets" both of individual companies and society as a whole. Commons sees the entire history of the US working-class movement as a growing understanding of the need to build industrial relations on the solidarity principle of "good will" and to create conditions that would help to maintain and realise the readiness for compromise.

Commons' theory reflected the ideology and practice of "business trade unionism" and promoted their "theoretical rationalisation". Like other bourgeois theorists of "industrial democracy", Commons believed that unions were the way to solve the problem of exploitation. There should be a system of rules, norms and statutes regulating the relations between capital and labour and stipulating their mutual rights and duties, a sort of "constitution" for "rational" industrial management.

In formulating his idea of attaining social accord through compromise, Commons takes the traditional bourgeois approach to the problem of clashing interests: that of "bargaining" or "checks and balances". Commons believed that by "institutionalising conflicts" that is, by bringing out and settling conflicts in an orderly manner with the use of definite procedures, it was possible to form a "truly social viewpoint" on various problems, a viewpoint expressing "the public interest" in contrast to the special interests of various social groups.

Faith in the principle of "social accord" and the belief that a wise national policy could be framed by balancing out contending interests are one of the most lasting illusions rooted in traditional liberalist philosophy. The idea is that any dispute can be settled either by agreement or by compromise; that the parties involved in the "bargaining" are independent from each other and are equal in strength; that state power is an independent, autonomous element of the system; that the decisions reached on the principle of checks and balances are truly wise; and that all the decisions taken are always implemented.

The institutionalists' posture is profoundly contradictory. On the one hand, they advocate the need for vigorous efforts to implement a constructive and purposeful state policy expressing the national interest. This implies the need for a strong political leadership, for normative economic guidelines, and a system of incentives and sanctions influencing the behaviour of economic agents. On the other hand, the institutionalists look to the checks and balances principle, which they see as a means of harmonising the contending forces in the economic and social sphere. They do not give any profound social analysis of the contradictions of present-day society, but always tend to overemphasise the factors and processes that could promote the tendency to harmony and stability.

In the 1970s, the growing social tensions, mass unemployment and inflation, the worsening energy, raw materials and ecological problems gave a new slant to the problem of social interests, tying it in with the question of priorities, national government policy and the need to set up an institutional mechanism which would make it possible to frame and implement a policy geared to national interests through purposeful influence on the investment process and income distribution. Attention now centred on planning state policy, raising the efficiency of the state sector and the state's regulating activity, and improving cooperation between the state and private business.

The goals and purposes of national indicative planning have been given a broader reading. Planning is now seen as a means of formulating and attaining definite meaningful goals of economic growth and implementing definite concepts for the development of the key sectors of the economy. The institutionalists assign an ever greater role to the normative aspects of planning, seeking to work out social criteria for assessing the utility and efficiency of social costs.

The institutionalist reading of evolution is marked by the idea that state power plays a positive role and that there are boundless possibilities for improving the mechanism of political democracy without political revolution or transformation of the basis of the capitalist system.

The institutionalists believe that the main purpose of political power is to create a favourable setting for the development of adaptational processes "from below", to guide, correct and supplement the mechanism engendered by the economic system itself.

In the 1950s and 1960s, when the growth of the capitalist economy was fairly sustained, the institutionalists not only shared the illusion about a new epoch of crisis-free, balanced development, but also vigorously elaborated industrialist concepts, proclaiming a new stage in social evolution, under which it was no longer economic relations but science and technology that determined the specifics of the economic mechanism, its functioning and development. On the strength of that, they drew a conclusion on the waning role of ideology and politics: their belief was that the social problem would be solved "the natural way", in the course of further economic progress entailing an increase in national income per head of population.

Capitalist reality itself dispelled these illusions about predestined social progress against the background of economic growth, about an inevitable spontaneous movement towards a "genuine welfare state". Today, the main stake is on reform, on filling out state policy with new content. Thus, in putting forward his "general theory of reform",[1] J. K. Galbraith emphasises that the problem of state power presents the main difficulty. The state should not only be the chief subject, but also an object of reform. In accordance with the traditions of bourgeois political liberalism, Galbraith calls for an improvement of the political system through a democratisation of electoral procedures, for measures to develop constitutional legislation and perfect the whole decision-making process in the socio-economic sphere.

He attributes the decisive importance to changes in popular mentality, regarding education as an instrument for "emancipating" popular belief and moulding a public consciousness corresponding to the conditions and requirements of present-day society. Galbraith seeks to present his theory as

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[1] John Kenneth Galbraith, *Economics and the Public Purpose*, Houghton Mifflin Company, Boston, 1973.

a "general strategy" for rational social action, as a platform for uniting virtually the whole of society. In effect, he appeals to the whole nation, to its "common sense", hoping to "free" men's minds from the fetters of "economic and ideological belief". He is particularly hopeful that a feeling of social responsibility will develop among the intelligentsia.

The idea of gradual reform is one of the main features of the institutionalist theory of social development. Social evolution is seen as a cumulative process, where the initial impulse generates changes in production, which in turn enhance the effect of the initial factor. This will ensure progressive development, in the course of which the system develops in qualitative terms. Where development is evolutionary, J. M. Clark wrote, the pace and nature of the changes are determined by what the system is prepared to accept, to what it can adapt in any given period. Evolution leads to "a 'mixed system', with a gradual change in the proportions of the mixture, until—if private enterprise is to give way to collectivism—the public sector might be in a position to take over the major economic functions without shock".[1]

The institutionalists believe that gradual reform can obviate the traditional alternative: "capitalism or socialism?" Development will proceed through intermediate stages, when old institutional forms are filled out with new content. As Clark put it, the correlation of public and private forces is not a fixed balance, but an evolutionary process of creative adaptation operating in the zone between full-scale *laissez-faire* and "full-scale collectivism".[2] This process amounts to an ever greater "socialisation" of functions relating to the allocation and use of economic resources and incomes formation.

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[1] John M. Clark, *Guideposts in Time of Change*, p. 64.
[2] John M.Clark, *Economic Institution and Human Welfare*.

The "third way" is an attempt to overcome the "dichotomy" of capitalism and socialism, to "amalgamate" the private market element in the economy with the centralised, planning element. Thus, speaking of the need to extend planning, with the orbit of private business shrinking drastically, R. Heilbroner draws the conclusion that the further development of the "mixed economy" would entail the convergence of the two types of economic regulation: the market mechanism and centralised planning. The gradual spread of planning to every aspect of economic life and the further accumulation of "collectivist" features, he says, will carry the US social system beyond the framework of capitalism. This is a definite prospect, which, Heilbroner believes, will mean as great a qualitative leap forward in comparison with the present system as the leap forward separating modern America from its colonial past.[1]

In forecasting the nature and direction of the evolution, the institutionalists follow J. A. Schumpeter's concept on the gradual withering away of private-enterprise capitalism and erosion of the bourgeois system of values. That concept had a powerful influence on the formation of institutionalist theories of post-industrial society, predicting the decline of the "business civilisation" with its principle of profit-making. These theories of capitalism's inevitable transformation into a "post-capitalist" society are contrasted with the Marxist theory of socialist revolution.

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[1] R. Heilbroner, A. Singer, *Economic Transformation of America*, Vintage Books, New York, 1977.

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CHAPTER EIGHT

ATTEMPTS TO SOCIOLOGISE BOURGEOIS POLITICAL ECONOMY: THE FRENCH SCHOOL

After the Second World War, British and US schools and trends gained the upper hand in bourgeois political economy, with the main centre for obvious reasons shifting from Britain to the United States. The French school, where the prevalent trend was sociological, became the third most influential school.

French bourgeois political economy was naturally influenced by the Keynesians and neoclassics. But in France, that process did not suppress or push into the background trends of French origin and, for various objective and subjective reasons, led to these complex results.

On the one hand, wide use of neoclassical and neo-Keynesian analysis instruments led to an influential economic-mathematical trend.

On the other hand, a group of French economists were dissatisfied with the much too abstract approach of the neoclassics and the mechanistic attitude of the Keynesians. From the outset, these French economists took a very reserved view of the conceptual principles and methodological premises of neoclassicism and neo-Keynesianism, and did their utmost to develop their own methodology of economic analysis based on an evaluation of the processes unfolding in the social relations between groups of people with respect to production and distribution of the social product.

Since these French economists focussed their attention on one specific link in the economic causal nexus—the behaviour and mutual relations between people grouped by social status or common interests—this trend may be called "sociological".

1. The Sociological Trend

The sociological trend, while being a natural product of the specific development of French capitalism, can hardly be described as a full-fledged school, although it has some elements of a school, considering the strong influence of Academician François Perroux on many economists of that trend. Perroux prefers to call his followers (those who do not reduce economics solely to an analysis of the operation of the market mechanism) as belonging to the modern trend in economic studies.

Why is it that in France the sociological trend in bourgeois political economy became predominant?

The reasons lie both in the specific features of France's socio-economic development and in the traditions of French philosophical and economic thinking.

In the late 18th century, France became an arena of bitter class struggle, which intruded into the studies of French bourgeois economists much more often than into those of their Anglo-Saxon colleagues, and made them think about the role of the relations between social groups in the economy.

The fact that French economic thinking was not as active in exploring the economics of individual enterprises and the laws of their behaviour was due to another peculiarity of the French society: the much greater role played by the state and the administrative apparatus in the country's economic life. French economists have traditionally been employed as government advisers on fiscal or budget matters, and not as marketing or investment advisers to private companies. Moreover, up until the Second World War it was considered a sign of bad breeding in academic circles to deal with problems of private profit. State finances, on the other hand, were as categorically assessed as an emanation of the public weal. The macroeconomic approach, which can be traced back to François Quesnay's economic tables, is a traditional feature of French bourgeois economic thinking, where it has always had sociological overtones, for the problems of state finances, taxes and expenditures naturally call for analysis of distribution and redistribution of incomes between social groups, strata, and classes.

Sociologically minded economists start from the assumption that to understand the economic mechanism one has to take into account all the elements of social life, the environment and human nature that have any relation to the reproduction of the material product and non-material services which provide the basis for the reproduction of man himself and his social institutions.

Since sociological economists have deliberately borrowed from related sciences and political economic trends, the sociological trend, like any other eclectic line of thought, stands more or less apart from every other line of bourgeois political economy rather than in opposition to these, or, to be more precise, intersects with these in varying degree. Sociological economists come closest to historical and institutionalist economists.

Sociological economists are most closely connected with the theory and practice of state-monopoly programming in France. It was they who formulated the ideological principles of dirigisme in the 1940s and 1950s, and still play a prominent part in the agencies that develop economic programmes. Involvement in the process of state-monopoly regulation leaves a strong pragmatic imprint on the views of sociological economists.

The "kinship" between the advocates of sociological economics in France manifests itself on the surface of things in a most specific form: in their attitude to its most prominent exponent, François Perroux, who in his numerous works formulated and reflected the whole spectrum of problems falling within the compass of the sociological trend, introduced a number of categories which were later on adopted as basic by other economists, and has done more than anyone else to spread the ideas of his followers and fellow-thinkers.

Among those who maintained or still maintain direct and regular contacts with Perroux are many prominent French economists: H. Bartole, G. Destanne de Bernis, J. Boudeville, M. Byé, J. Weiller, J. Denizet, F. Sellier, H. Chambre. At the same time, the sociological trend includes many other researchers who are well known in France and abroad, like François Bloch-Lainé, Claude Gruson, P. Dieterlen, J. Lecaillon, A. Marchal, P. Massé, J. P. Mockers, J. Houssiaux, P. Uri. In their method and approach to economic science, they come quite close to Perroux's concept, although their views are not directly dependent on his ideas. Still, to characterise the most typical features of the sociological trend, we shall concentrate on the system of views advocated by Perroux as the most representative economist of that trend.

The whole of Perroux's research (in the past few years, at any rate) has one aim in view: to develop a new "general theory of equilibrium", which would be as convincingly formalised as Léon Walras's theory but, instead of being based on the principles of perfect competition, would start from different assumptions better reflecting present-day capitalist reality with the monopolies, the state, and the trade unions. According to Perroux, this should be a "generalised" theory, in which Walras's equations would be only a special case.

Perroux makes a point of not leaving out a single section of the "general theory", exploring virtually the whole range of political and economic problems. In the past 50 years, he published something like 50 volumes and 500 articles.

Perroux's "general theory of equilibrium" is not pivoted on the market, but on "social structures" characterising the relations in the sphere of production and distribution. These relations can be cognised through the market, where they manifest themselves in the marketing of the product.

Perroux maintains that the movements of commodities are in the final count determined by some essential relations, or "steady structures". He says: "The global flows of commodities and incomes are relays leading to behaviour, projects, and plans."[1]

Perroux's concept of "economic structure" has no socially distinct, class contours and this makes his definition of that category much too hazy and abstract.

> "The structure of an economic ensemble is determined by the *set of ties* that unite the simple and complex units, and *series of proportions* between the flows and between the stocks of elementary units and objectively significant combinations of these units."[2]

Since the two sets are fairly stable and change slower than other variables, they can serve as a framework (parameters) for describing economic reality. Perroux does not analyse the reasons behind the stability of these structures, but emphasises

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[1] François Perroux, *L'Économie du XXe siècle*, Presses Universitaires de France, Paris, 1961, p. 11.

[2] *Ibid.*, p. 285.

their quantitative, statistical reality and simply states the fact that it changes very slowly over a definite period. At the same time, he maintains that the explanation of the specifics of the structures is to be located in their qualitative peculiarities, that is, in the sphere of human relations. He says that the patterns of the flows of goods and services

> "at any given moment can be seen as the consequence of preceding social struggle and a cause of the ongoing social struggle".[1]

"Economic structures", Perroux believes, are primarily a "power grid" of relations between unequal economic agents, who do not build their economic ties according to abstract market laws or depending on the free play of supply and demand, but actively form the "economic space", that is, the amount of goods and their prices.

These structures have the important property of stability: they depend very little on current changes in the supply of commodities and their prices (i.e. on relations in the sphere of commodity exchange), on short-term and cyclical fluctuations in production. At the same time, these structures are also resistant to any deliberate attempts by individual economic agents, social groups or political authorities to change them. They are a product of collective action, a product of struggle, competition, rivalry, conflicts, and cooperation. They are wider than the statistical indicators characterising commodity flows. These structures consist, in part, of invisible grids which are hard to evaluate: flows of technical and economic information, grids for exercising power, and grids of the agents' plans and projects. All these cannot be put into figures, but can only make themselves felt by influencing those magnitudes that can be evaluated.

Perroux takes a mechanistic view of the structures, without attempting to divide these into primary

[1] *Ibid.*, pp. 283-284.

and secondary, essential and unessential, dominant and subordinate.

A point to note, however, is that the structures doctrine shows the attempts of sociological economists to go beyond the framework of market relations and include a phenomenon which the neoclassics regard as sociological within the sphere of political economy. Perroux writes that "the struggle between agents and their groups for possession and use of things that can be evaluated belongs to the economic sphere".[1]

Sociological economists differ in their interpretation and especially in their assessment of the importance of various structures. J. P. Mockers,[2] for instance, maintains that the crucial production structure in the modern economy is the "planning state", which is the most powerful, dominant group subordinating the behaviour of other groups to its own will. Pierre Dieterlen justly remarked in this context:

> "Alas! The capitalist state ... in spite of the evangelical texts of its good apostles, remains a screen-group meant to throw a convenient veil of democratic planning over the activity of the truly dominant groups which are to be found elsewhere."[3]

In spelling out the meaning of the phrase, "dominant groups which are to be found elsewhere", Perroux remarked in one of his articles that although it is hard to say of whom the groups enjoying real power consist, it is nevertheless obvious that

> "a handful of persons are in command of vast material and human resources" and that

[1] François Perroux, *op. cit.*, p. 372.

[2] Jean Pierre Mockers, *Dynamique et structures. La méthode structurale comme fondement de l'analyse dynamique en économie*, Editions Sirey, Paris, 1966.

[3] *Revue d'économie politique*, No. 2, March-April 1966, p. 335.

> "probably, these super-entrepreneurs are either financiers themselves or depend on highly concentrated financial power".[1]

This statement can be interpreted as indirect recognition of the fact that the financial oligarchy, finance capital, is the "dominant structure", the truly dominant social group in the modern capitalist economy.

The main structural element of Perroux's "generalised theory of equilibrium" is the macrounit, a stable systemically organised association of producers. The main difference of Perroux's theory from the Walras-Pareto theory of equilibrium is that the former is pivoted on an "active" economic agent.

The Walras-Pareto theory starts from the assumption that economic agents are equal and fully independent, and are guided in all their actions solely by the price; that their behaviour is motivated solely by the elementary rules of maximisation, which simply determine the volume of supply and demand, and the price of equilibrium. As Perroux points out, that theory does not deal with extra-market relations or groups as organised aggregations of economic units (and the agents behind these). Walras-Pareto's general equilibrium

> "does not describe a *steady state*, but a state that any sociologist would consider *contradictory*, because in constructing a scientific model the sociologist never starts from premises that are in direct contradiction with the most essential, irremovable conditions of the behaviour of human agents, of subjects."[2]

That is why, Perroux goes on, in modifying the theory of general equilibrium, one has to discard

[1] *Giornale degli economisti e annali di economia*, Nos. 5-6, 1965, p. 339.
[2] François Perroux, *op. cit.*, p. 23.

its premises altogether and replace these with new ones.

Perroux believes that the first and initially unnoticed step to undermine the theory of general equilibrium was taken by Edward Chamberlin, when he analysed advertising inputs as part of his theory of monopoly competition. In the course of his analysis, Chamberlin tacitly recognised that the firm can influence the surrounding "economic space" by making additional inputs. This logically entailed the introduction into economic analysis of a distinction between production inputs, marketing inputs, and inputs for the transformation of the surrounding "economic space". From this it also naturally follows that the economic positions and opportunities of individual firms are unequal and that these can be divided into "active" (exerting influence) and "passive" (subject to influence). This also means, Perroux points out, that the market flows of goods and services are supplemented with extra-market flows of "influence" which make up "power relations".

These power relations do not affect the instant equilibrium of commodity exchange: at any given moment, this exchange is carried out in accordance with the limitations created earlier on in the course of struggle between economic agents. Perroux writes:

> "The most competitive market forms, if one departs from the model of perfect competition, cannot be defined or understood unless one takes into consideration the balance of power between social groups."[1]

In other words, in introducing the time factor into the equilibrium models, Perroux notes that all the parameters of the models are formed under the influence of the power balance between the economic agents, "bearing an imprint of power relations".

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[1] François Perroux, *op. cit.*, pp. 32-33.

This applies both to relations in the distribution of incomes and initial stocks of commodities and production factors, and "maximisation psychology" (i.e. determination of the concrete goal of activity: profit, personal gains, and so forth).

Power, Perroux believes, is present in all operations, both on monopoly markets and in extra-market relations, using two typical methods of influence: information (by limiting or supplying this to its own advantage) and constraints (by contriving scarcities of values). Such power of one economic agent over another can take the form of influence, leadership, partial or total subjugation.

> "One will note that power originates and is exercised within an organised whole. This fact, unanimously recognised in present-day sociology, is incompatible with the Walras-Pareto equilibrium, but easily fits into the generalised theory of equilibrium we suggest."[1]

That is why the group, or "macrounit", is the fundamental component of Perroux's "generalised theory", the basic parameter of his model.

Groups, says Perroux, are "constellations" of unequal economic units (agents), within which hierarchic relations have taken shape. Groups can be evident, latent, temporary, and stable. Stable groups gather around a leader-unit, which has the power and opportunity to change the structure, growth rate or type of organisation of other units.

The national economy, says Perroux, can be seen as an organised aggregation of simple and complex units headed by the state, a decision-making centre, which turns the whole aggregation into a large macrounit, putting in order the system of influences and power relations relying on its own strength. The state's task, Perroux believes, is to

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[1] *Ibid.*, p. 37.

arrange and regulate power relations in the interests of society as a whole.

> "Under the influence of competition between groups and between unequal firms, and also under the influence of the information being spread and the power being exercised by the representatives of collective interests, including the state, one will discern a certain controlled and more or less humanised order of rivalry and competition between individuals and groups over the use of values."[1]

Perroux regards his general equilibrium model as an instance of the use in economic analysis of the phenomena of influence and coercion, a methodological device within the "broad stream both of economic and sociological thought".[2]

Henri Aujac's theory of inflation is another example of the use of the economico-sociological method in economic analysis. It was formulated back in 1950,[3] but is still relevant today. It attracted particular notice in the 1970s, when a heavy tide of inflation swept across the capitalist world.

Aujac disagreed with the view that inflation developed as a result of disturbances in the monetary sphere and influenced the social sphere, but maintained that these disturbances themselves were due to the peculiarities of the relations between social groups and their behaviour. Here is how he formulated his basic proposition: "Inflation is the monetary consequence of the behaviour of social groups."[4] Inflation is triggered off when the dominant social group switches from "adaptation behaviour" to "rejection behaviour" and seeks to change the

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[1] François Perroux, *op. cit.*, p. 57.

[2] *Ibid.*, p. 52.

[3] Henri Aujac, "L'influence du comportement des groupes sociaux sur le développement d'une inflation". In: *Économie appliquée*, No. 2, 1950, pp. 279-300.

[4] *Ibid.*, p. 281.

monetary relations between the groups in its favour instead of adapting to these in the usual passive way.

In effect, Aujac examines the struggle over the share of the income realised by various social groups. In the course of this struggle, employers sometimes resort to price rises, and workers seek to raise their nominal wages. The mechanism of money and credit circulation adapts itself to the struggle between social groups and acts as intermediary in that struggle, following in the wake of price rises.

So, Aujac's inflation theory elaborates Perroux's ideas on the priority of human action over mechanistic market factors, on the ability of dominant groups to change, by applying their power, the surrounding economic space in their own interests, so inducing the other agents to adjust their plans and intentions to the new parameters.

Jean Marchal's views on the distribution of the national income come close to Aujac's position. He starts from the assumption that the ultimate goal of the social group's behaviour (and struggle) is to obtain a definite share of the national income. That is why, Marchal maintains, price rises (in the interests of the employers) or wage increases (in the interests of the workers) are a means of ensuring the desired level of income. Advocates of this approach overrate the importance of redistributive operations for explaining the mechanism of inflation and, what is particularly important, see this mechanism as much too subjective. They underestimate the role played by the social group, or class, in the sphere of production, centering on its activity in the sphere of distribution.

In this way, they give distribution priority over production, so unjustifiably reversing the direction of causal ties between production and distribution.

While objectivising the sphere of social relations and including it in economic analysis, the representatives of the sociological trend nevertheless present an embellished and, consequently, distorted picture of the class struggle in present-day capitalist society. They use categories like "struggle-rivalry" and "conflict-cooperation" to create the impression that the interests of all the economic agents in the contemporary social economy (including those of the working people and the owners of capital) are immanently the same. While regarding the struggle between classes and groups as a dynamising element of economic life, they deny the antagonistic, irreconcilable nature of that struggle and recognise only its "economically beneficial aspect".

The sociological trend is essentially "optimistic" from the capitalist viewpoint, for it proclaims the idea of constant and inevitable evolution towards a better and more humane society, where production will not be run on the principle of "profit maximisation", but with a view to the interests of Man with a capital M, man as an abstract perfection. This evolution is to be ensured, sociological economists maintain, by the bourgeois state and the creative endeavour of a handful of scientists: the state is to be the arbiter, regulating power relations in the interests of the "public weal" (the French version of the Anglo-Saxon "welfare state"), and the scientists are to develop the model of a future conflict-free society and point out the best ways to build it. In this way, objective analysis ultimately gives way to a pious hope.

The sociological trend in French bourgeois political economy eulogises the decisive role of the state in the system of state-monopoly capitalism, and it is not surprising that this form of apologetics has developed in France, where various forms of state-monopoly regulation are being used on a particularly large scale.

2. Evolution of Neoclassical Ideas

In spite of the strong "sociological tradition" in French political economy, as it was pointed out above, the neoclassical trend has retained its importance. In that country of developed state-monopoly capitalism, it reflects the ideology of those bourgeois circles which seek to limit state intervention in the economy to the sphere of market relations. That trend of bourgeois political economy also to some extent reflects the urge of the monopoly bourgeoisie to strengthen the positions of private capitalist property and to prove that private capital is capable of social manoeuvring necessitated by the spirit of the times and the growing strength of the working-class movement.

The positions of the neoclassical trend in French bourgeois political economy did not remain unchanged. Up to the 1960s, the neoclassical doctrine had had few followers in France. In the 1960s, its positions strengthened, and France became the scene of what Western economists called a "neoclassical resurgence". That resurgence, however, did not last very long and in the mid-1970s waned perceptibly. As the economic difficulties mounted, one could not fail to see the artificial nature of the theoretical constructs of the neoclassical school, which now faces another grave crisis.

The postwar development of the neoclassical school in France could be divided into two stages.

The most prominent representatives of the "first generation" of neoclassics (Jacques Rueff and Maurice Allais) took an active stand against the growing influence of Keynesian and dirigist concepts embodied in programmes for the state-monopoly regulation of the economy. In contrast to the dirigists, they believed that the free play of market forces was more reliable than programming in establishing and maintaining an equilibrium. They believed that any change in demand was instantly reflected in the structure of relative prices, something that signals an immediate intersectoral transfer of production factors. In other words, the price mechanism quickly generated forces that restored the competitive equilibrium, which the neoclassics saw as the economic optimum.

The postulates behind the neoclassics' marginalist models prevented a realistic understanding of the contradictions of capitalist reproduction and inevitably led to a superficial, purely monetarist concept of the capitalist cycle.

The practical recommendations of the neoclassics (or the neoliberals, as they called themselves) reduced the state's economic functions to a minimum, so retaining many features of earlier liberal concepts. At the same time, Rueff and Allais discarded the sterile dogma of *laissez-faire* and, in contrast to the old liberals, who saw the state as a passive onlooker, wanted the state to organise the operation of the price mechanism.

The neoclassics could not fail to note that the market was often unable to solve the problems of realisation and employment. But they explained such "irregularities" by the existence of artificial barriers in the way of the free movement of prices.[1] For the distortion of the market mechanism, the neoclassics blamed the various forms of "market organisation" (cartels, trusts, trade unions) and the state, whose systematic intervention in the economy, they believed, particularly jeopardised the institution of private property and "consumer sovereignty". That is why they sought to prove the need to reduce the state to the level of a rank-and-file partner

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[1] Jacques Rueff, for instance, believed that lasting unemployment could only arise when wages were fixed at a level exceeding the "equilibrium" level, that is, the level determined by supply and demand. In the 1920s, he discovered a direct dependence between the movement of real wages and the rate of unemployment, which came to be known as the Rueff Law.

in the exchange, functioning largely in accordance with conventional microeconomic criteria.

Such an approach showed that its advocates refused to see the objective laws of capitalist development at the monopoly stage. The conclusion they drew from the fact that reality did not fit into the stereotypes of "perfect" competition was "so much the worse for reality". They recommended that reality should be adjusted in every way to the characteristics of the ideal market. The state, they believed, had to take vigorous steps to cultivate and organise competition.

Moreover, the neoliberals admitted the usefulness of state action aimed at ensuring the stability of the general price level and at combatting inflation, for the latter, they believed, undermined the effectiveness of the market mechanism by enhancing the uncertainty in economic computations. Since Rueff and Allais located the reasons for the fluctuations in the general price level solely in the monetary sphere, they advocated monetary regulation of the economy as the universal instrument. Rueff, in particular, urged the state to give up its policy of maintaining the interest on treasury bills, which imparted one-way elasticity to money circulation and was, he believed, the main cause of inflation.[1] Allais's practical recommendations also boiled down to credit control.[2]

But the recipes for moderate credit and money regulation could not cure France of its postwar economic difficulties. The ruling class had to look to other, non-market mechanisms for stepping up economic growth. It was the dirigists who got the upper hand in the decision-making centres (Com-

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[1] See: J. Rueff, *La régulation monétaire et le problème institutionnel de la monnaie*, Paris, 1953; also his, "La restauration du franc". In: *Revue d'économie politique*, 1960, No. 6.

[2] See: M. Allais, *Économie et intérêt*, Librairie des publications officielles, Paris, 1947, Vol. 2, pp. 579-580.

missariat for Planning, the Ministry of Finances, etc.). Their idea was that the state should perform entrepreneurial functions and play an active role in the flow of capital from one sphere of the economy to another. These principles were put into practice in capitalist programming.

Throughout the 1940s and 1950s, the neoclassics had very little influence on the economic policy of state-monopoly capitalism and did not enjoy wide recognition in French academic circles.[1]

The neoclassics began to exert a marked influence on the strategy of the ruling circles in the 1960s, when a fairly influential trend known as the "new French school" took shape in French political economy. Its representatives (Edmond Malinvaud, Gerhard Colm, T. Montbrial, Lionel Stoleru, and others) accepted the basic neoclassical premises.

The growing popularity of neoclassical ideas was due to changes on the economic scene. By that time, French capitalism to some extent managed to smooth away the worst economic disproportions and markedly to renew and expand the country's production facilities. On the other hand, as tariff barriers were lowered and economic internationalisation increased, competition became an important factor influencing the rate and proportions of reproduction. All this gave rise to illusions that the French economy had moved so close to a state of equilibrium that "natural" market forces had to play the main role in maintaining that equilibrium. The implementation of some neoclassical recommendations was also due to the fact that the

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[1] André Marchal pointed out that the state's macroeconomic policy did not follow the recommendations of the neoclassical school and emphasised the weakness of the stand taken by the French neoclassics, whom he described as a "handful of engineers indulging in the joys of pure economics". (André Marchal, *Méthode scientifique et science économique*, Editions M. Th. Génin, Paris, 1952-1953, Vol. 1, p. 149.)

private-monopoly element in the French economy had consolidated its positions. Big Business, which demanded a "free hand" in the economy, now had a solid material and organisational basis to rely upon as a result of the greater production and financial concentration of capital. The neoclassical recipes coincided with and ultimately expressed the interests of the strengthened monopolies, which were prepared to carry on an independent competitive struggle.

In the 1960s, the neoclassics consolidated their positions throughout bourgeois political economy as a whole. In France, this process took a specific form, for the neoclassics in that country had to face a less uniform opposition (from the standpoint of method), which included both Keynesians (dirigists) and sociologically-minded economists. That is why in its call for a "methodological renewal", the "new French school" from the very beginning emerged as the antipode of the sociological trend. In criticising the sociological economists for their "incoherent" and descriptive concepts, the "second generation" neoclassics have been vigorously introducing a set of formal instruments for economic analysis that is traditional for Western (primarily US) economic science. It is hardly a coincidence that many representatives of the "new French school" studied economics in the United States.

But for the neoclassics, the well-justified demand for a strictly logical and non-contradictory theory becomes an end in itself.

First, in their urge to simplify reality to the utmost and reduce it to a set of universal laws they tend to supplant the real economy with an abstract model which has little in common with the concrete historical formation. Their models fall within the range of what Marx called vulgar political economy, which ignores all the conditions of capitalist production and denies "all its principles and specific features—in short *capitalist production* itself".[1] The neoclassics' asocial schemes, which obscure the relations of exploitation and class contradictions, present an apologetic picture of bourgeois society.

Second, the method used is much too complicated for an adequate qualitative analysis. Representatives of the "new French school" often confine their research to the purely mathematical properties of the model, inviting the reader himself to fill it out with economic content.

Finally, the inadequacy of the neoclassics' initial postulates, which do not reflect the substance of the economic process, stands out very clearly against the background of their constant attempts to refine their formal devices.

A point to note is that the neoclassics themselves take a fairly sceptical view of the correspondence between their postulates and the actual conditions.[2] They often make rigid assumptions in order to be able to use mathematical methods or for other, purely formal reasons. Taking an extremely rationalist stand, the neoclassics contrast their logical schemes with concrete reality.

The neoclassics did not confine themselves to "pure" theory and extended their activity to the practical regulation of the economy. Combining academic careers with posts of government advisers, representatives of the "new French school" helped to frame the state's economic policy. In this area, too, the French version of the "neoclassical resurgence" has its specific features. Thus, in the United States, the neoclassical defence of the private-enterprise system took the form of the monetarist

[1] Karl Marx, *Theories of Surplus-Value*, Part II, p. 501.

[2] In one of his works, which, according to the author, summarises nearly 20 years of research in the theory of capital, M. Allais admits that of the seven major neoclassical hypotheses only "Hypothesis 3 is a very strong one". (M. Allais, "Some Analytical and Practical Aspects of the Theory of Capital". In: *Activity Analysis in the Theory of Growth and Planning*, Macmillan, London, 1967, p. 80.)

assertion about the stability of the capitalist economy, and in France, with its extensive nationalised sector and economic programming, the same task called for different arguments. The French neoclassics insist, in the first place, that private business and the market can ensure the optimal distribution of resources, and from this angle sharply criticise the state's direct intervention in reproduction that is characteristic of France. The revision of the principles of economic policy in the second half of the 1960s and the early 1970s was largely carried out with a view to the recommendations formulated by the "new French school". In the course of that revision, some state-monopoly forms of economic management were replaced with market and private-monopoly regulation. The state increasingly resorted to indirect instruments of economic control.

That line was synthetically expressed in the changes in the approach to programming. In the years of the fifth (1966-70) and sixth (1971-75) plans for economic and social development, the ruling circles reconsidered their attitude to the place and role of planning in the French economy. Before that, "coordination" (exchange of information among all the agents of the reproduction process and concerted action in framing economic programmes) was seen as the crucial element of "indicative planning".[1]

The "coordinated economy" concept, which was in tune with the principles of the sociological school, recognised that the interests of the agents of the capitalist economy were inherently contradictory, but could be "dovetailed" through a joint

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[1] One of the architects of "indicative planning", the French economist P. Massé emphasised that the drafting of the plan was of greater importance than the plan itself. (J. McArthur, B. Scott, *Industrial Planning in France*, Harvard University, Boston, 1969, p. XVIII.)

effort on the part of the market forces and programming.

The neoclassics take a fundamentally different view, maintaining that under a "competitive" setup, the spontaneous action of economic agents yields the best results. They reproach programming for a grave violation of the market "rules of the game" and regard "coordination" as something of a "monopoly deal". Under the neoclassical approach, coordination of interests is not only superfluous, but even harmful. Such views filtered into the regulating state bodies and, in the course of the drafting of the sixth plan, "coordination" degenerated into a mere formality. This is due, in particular, to the extension of the sphere of market relations.

Simultaneously, the range of centrally directed economic processes is narrowing down. Thus, sectoral projects are no longer being covered by the plan. The state refuses to take a systematic part in forming the sectoral rate of profit and economic structure, seeking to regulate the dynamics of the most aggregated indicators: industrial production, employment, prices, and so forth. The choice of an appropriate "balanced" version of growth in effect becomes the prerogative of private monopolies and financial groups.

The economic instruments for ensuring the attainment of plan targets are also changing. In the past, taxation and credit policy was selective, to some extent promoting the extra-market distribution of financial resources in accordance with the priorities written into the plan. By the 1970s, however, the elements of centralised distribution in the credit and financial systems had virtually disappeared, and the funds being accumulated in these are increasingly at the disposal of the monopolies.

But the objective laws of the capitalist mode of production, which gave rise to the sharp structural disproportions, aggravated the environmental problem, worsened the "quality of life", and caused other crisis phenomena in the French economy in the mid-1970s, insistently demand centralised regulation. In the atmosphere of the galloping inflation of the 1970s, which laid bare the class antagonisms of bourgeois society, the neoclassics' attempts to "apply" their asocial schemes to the real economy are evidently quite groundless.

In these conditions, the neoclassical trend found itself in a state of deep crisis. The practical recipes offered by the neoclassics also proved to be invalid. The crisis that spread across the capitalist economy in the mid-1970s induced the French ruling circles to start another review of the principles of economic policy.

CHAPTER NINE

STRUCTURAL CHANGES IN THE ECONOMY OF CAPITALISM AND THEORIES OF ITS SOCIAL TRANSFORMATION

In this chapter, we consider the two varieties of bourgeois-reformist concepts which seek to prove that capitalism can be transformed within its own framework.

Concepts of the first variety developed on the basis of traditional theories envisaging the possibility of toning down the class contradictions of capitalism through a gradual "equalisation of income" both at a microeconomic level (as a result of measures taken by the firm) and at a macroeconomic level (with the help of fiscal and budget policy). These concepts, variously modified, are still predominant in present-day vulgar economics.

Bourgeois-reformist concepts of the other variety aim to prove the possibility of transforming within the capitalist framework society's class structure itself, that is, of carrying out its social transformation in the direct sense of the word. The emergence of these concepts is tied in with the bourgeois-apologetic interpretation of the current scientific and technical revolution. Bourgeois economics gives an anti-Marxist interpretation of the profound changes brought about by this revolution in the sectoral structure of the economy and the occupational make-up of the population, in the development of capitalist socialisation of production in its two forms: both at individual enterprises and on the basis of growing social division of labour.

The scientific and technical revolution has markedly intensified the state-monopoly regulation of the economy in individual countries and has promoted the development of international forms of such regulation. The international interlacing of capitals and the growing interconnection between the capitalist states under the international division of labour have given rise to various theories of capitalism's transformation aimed against the Marxist-Leninist analysis of the world revolutionary process.

To meet the so-called "socialist challenge" in the contest between the two systems, bourgeois ideologists have developed their latest theories on the transformation of capitalism. The fundamental changes in the balance of forces between the two systems, which are due to the victories scored by socialism in this contest, induce bourgeois economists to adjust to the new situation by adopting new methods of social manoeuvring in the intensifying class struggle both within individual countries and on the international scene.

One of the manifestations of the present-day class struggle on the ideological front is the confrontation between Marxist-Leninist political economy, which studies the deep-going uniformities of capitalism, and vulgar bourgeois economics, which makes use of superficial phenomena conditioned by the fetishist nature of capitalist relations of production. The problem of social equality between men is among the major problems where this confrontation of ideas is particularly pronounced.

Marxist-Leninist political economy studies the development of production relations and their interplay with the productive forces and the superstructure. Vulgar bourgeois economics seeks to vindicate capitalism not only by fetishising the bourgeois relations of production, which is the usual tendency under capitalism, but also by using the illusory notions engendered by the progress of the productive forces and the seemingly above-class role of the bourgeois state. Such mystified notions of "objectivised" reality lie at the root of the theories of capitalist society's transformation we are considering. These theories are fairly flexible in adjusting to the changing reality. This is particularly evident with regard to the theories of "industrial" and "postindustrial" society, formulated under the present scientific and technical revolution and the state-monopoly regulation of the economy it entails.

1. Sources and Methodological Premises of the Theories of Capitalist Society's Transformation

The theories advocating social equality between men were first engendered by the bourgeois revolution.

During the French bourgeois revolution of 1789, the leaders of the third estate used the inspiring ideas of liberty, equality and fraternity as a political slogan in the class struggle against the rule of the aristocracy and the clergy. But once the bourgeoisie became the dominant class and betrayed the interests of its allies (peasants, handicraftsmen and workers), it had to look for methods of rooting out the seditious revolutionary view of the idea of equality and adapting it to the production relations and juridical norms of capitalist society.

The church, whose dogma is that all power derives from God, quickly adapted itself to acting as the ideological instrument of the dictatorship of capital. But it was unable to fill the vacuum that resulted from the collapse in the course of the bourgeois revolution of the feudal idea of the hierarchy of power, according to which the peoples were ruled by "the anointed". Atheism, which the French materialists—the champions of the Enlightenment, whose ideas paved the way for the revolution—did much to assert, spread widely in the working class.

But it was the Marxist teaching, the theoretical expression of the interests of the working class, that dealt the most crushing blow at the slave-holding and feudal doctrine of the "kingdom of heaven", which promised salvation for the torments of slave labour, poverty and rightlessness in this world. The Marxist teaching showed capitalism's role in creating the new productive forces based on science and technical progress, and proved that the proletariat was now the main productive and social force of capitalist society and that its historically conditioned mission was to overthrow the power of the bourgeoisie and build a classless communist society on the principles of genuine equality and fraternity.

In the mid-19th century, the spectre of communism and fear of a proletarian revolution induced the bourgeoisie to supplement its terroristic and police methods of struggle against the working-class movement with other methods, in order to disarm it in ideological terms by spreading reformist ideas denying the need for a revolutionary transformation of capitalist society.

Vulgar bourgeois economics played a vast and extremely dangerous role in formulating such reformist ideas, and the founders of Marxism fully took this into account. Thus, Marx's basic work, *Capital*, is subtitled "A Critique of Political Economy". In it, Marx not only brought out the economic laws of capitalist development, but also exposed the class substance of vulgar bourgeois political economy and its efforts to mystify reality. Simultaneously, Marx offers a brilliant example of the methodological approach to its criticism. He begins his *Capital* by characterising the objective basis which enables the vulgar political economy to mystify reality so as to veil the substance of capitalist exploitation and prove that the principles of freedom and equality are realised in bourgeois society.

The final paragraph of the first chapter of *Capital* (Volume One) is entitled "Commodity Fetishism and Its Secret". It is commodity fetishism that engenders the peculiar forms in which reality is reflected.

> "The categories of bourgeois economy consist of such like forms. They are forms of thought expressing with social validity the conditions and relations of a definite, historically determined mode of production, viz., the production of commodities. The whole mystery of commodities, all the magic and necromancy that surrounds the products of labour as long as they take the form of commodities, vanishes therefore, so soon as we come to other forms of production."[1]

This idea is very important, for in present-day capitalist society objective prerequisites still exist for veiling the substance of the working people's exploitation, and modern vulgar economics makes full use of this.

Under slavery and serfdom, exploitation was not disguised in any way. The slave knew that he and all his free time belonged to his master, who had taken him into slavery by right of conqueror or had bought him on the slave market. The serf knew how much time he had to work for the landowner and how much time and strength remained for himself and his own family. The proletarian, for his part, is allowed an illusory personal freedom,

[1] Karl Marx, *Capital*, Vol. I, Progress Publishers, Moscow, 1974, pp. 80-81.

and he realises it on the labour market, where he can choose an employer and conclude a seemingly equitable commodity transaction with the latter: the owner of the labour power does not sell himself, but only his capacity to work, while the capitalist, the owner of the capital, pays him an agreed wage. The proletarian retains these illusions even when he works at an enterprise with a severe barrack-room labour regime imposed by the capitalist. It seems to the proletarian that by his work he creates an income for himself and that the size of this income depends on his work.

One specific feature of apologetic bourgeois science is that its prophets, robed in academic mantles, seek to spread ideas that are meant to ensure the spiritual enslavement of the working people and their exploitation, to sustain the distorted, illusory notions that are engendered in the minds of those involved in production by the capitalist relations of production and are embodied in real categories expressing these relations. These illusions have proved to be as persistent as religious myths. As a category of apologetic economics, they are an instrument for inculcating false notions of reality into the minds of the working people.

Wages are one of the most important real categories that give rise to mystified notions of reality, a category which is particularly popular in vulgar economics.[1] Wages paid to the seller of the labour power give him the illusion that all his work in production is fully paid for. This category also entails a mystified view of the capitalist's profit, which, being a converted form of usurped surplus value, that is, of the worker's unpaid labour,

[1] "This phenomenal form, which makes the actual relation invisible, and, indeed, shows the direct opposite of that relation, forms the basis of all the juridical notions of both labourer and capitalist, of all the mystifications of the capitalistic mode of production, of all its illusions as to liberty, of all the apologetic shifts of the vulgar economists." (Karl Marx, *Capital*, Vol. I, pp. 505-506).

appears to be the product of capital itself. It is not the consumed living labour embodied in the means of production used by the capitalists but these means of exploitation themselves that appear to be the main productive force that creates society's wealth, and the capitalist who owns these means appears to be the rightful owner of this wealth.

This contrast between past labour embodied in the means of production and living labour, of which the worker himself is the vehicle, lies at the basis of the concept which puts a technological interpretation on the productive forces and is widely used by vulgar economists in their theories of the social transformation of capitalism. Ever since the 1830s, they have been using a technological, rather than a social characterisation of the productive forces to justify capital's right to exploit labour.

That is basic to all technological and technocratic concepts not just in some individual school of vulgar bourgeois economics, but in all of them. While glorifying the power of capital, vulgar economists regard the worker solely as one of the material factors of production used by the owner of the instruments of labour as a component of the technological process alongside machinery and raw materials. On the basis of the theory of production factors, they have elaborated a theory of income distribution which does not even mention class antagonisms. This theory, which regards income as the result of three factors of production—capital, land and labour—is still alive, having undergone definite transformations, but retaining its substance: it says that the worker's income depends on capital's "life-giving force", and that the worker should be grateful to capital for his daily bread.

That concept of income gave rise to the most primitive forms of "bourgeois socialism", which maintains, as the *Manifesto of the Communist Party* pointed out, that "the bourgeois is a bourgeois—for the benefit of the working class".[1] As a pseudo-science, this "bourgeois socialism" has survived until our day, retaining its importance as an instrument of bourgeois apologetics used by monopoly capital.

Vulgar economics rejects the Marxist thesis that capitalist exploitation exercised in production, that is, in the sphere where surplus value is created, predetermines the nature of the distribution of material wealth. On the strength of the seemingly separate functioning of the various forms of capital, it seeks to prove that the sphere of distribution is independent from the sphere of production. Hence the conclusion that reforms in the sphere of distribution can eliminate the class antagonisms arising in the sphere of production.

That apologetic concept was first formulated by John Stuart Mill, the last representative of classical bourgeois political economy, whose views, Marx wrote, reflected the "bankruptcy of bourgeois political economy". In contrast to the cynical apologists of capital who advocated coercion, Mill called for reform. Marx ranked him among the economists who "tried to harmonise the Political Economy of capital with the claims, no longer to be ignored, of the proletariat".[2] Mill tried to piece together some elements of Ricardo's theory of value with the reformist theory of the redistribution of incomes.

But when Marxism, among whose sources was Smith's and Ricardo's labour theory of value, spread within the working-class movement, even Mill's half-hearted recognition of that theory became dangerous for bourgeois apologists.

In the 1870s, marginalism, or the theory of marginal utility, became the theoretical basis for apologetic anti-Marxist concepts of a "fair" distri-

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[1] Karl Marx and Frederick Engels, *Collected Works*, Vol. 6, p. 514.

[2] Karl Marx, *Capital*, Vol. I, p. 25.

bution of income. It was meant to substitute subjective psychological factors for the labour theory of value.

Instead of analysing the influence of production on the market, marginalism centred economic research on the market influence on production. In contrast to Marxism it explained such ills of bourgeois society as crises and unemployment by the imperfections of market structures, rather than by the relations of production peculiar to that society and based on capitalist property in the means of production.

The theory of marginal productivity of capital, which marked a new stage in the development of marginalism in the late 19th century, not only explains the wage level by the conditions of market competition, but seeks to prove that the workers employed at a capitalist enterprise have a vital concern in making it more competitive. So, the marginalists' aim is to prove that the distribution of incomes is determined by the random laws of the market which are beyond human control.

But the worsening of class contradictions and the growth of the working-class movement under the influence of socialist ideas increasingly undermined the incomes theory, which asserted that incomes were harmoniously distributed in spite of the widening gap between the unprecedented growth of monopoly bourgeoisie's wealth and the poverty of the masses. The bourgeois-reformist trend in vulgar economics came to recognise the need for some redistribution of incomes with the help of progressive taxation that would trim the gigantically swelling profits of the capitalists. But the modest encroachments on capitalist profits suggested by bourgeois-reformist theorists not for any humane reasons, but for fear of revolutionary upheavals that could be caused by the masses' protest against poverty and social injustice, were resisted by the more conservative theorists who believed, with

Malthus, that poverty was necessary if wealth was to grow.

The conservative forces in Britain, where bourgeois political economy originated, advocated imperialism for purposes of social demagogy. Joseph Chamberlain, one of the most prominent ideologists of imperialism, sought to prove that the only way to root out poverty in Britain was to obtain new markets.

The Great October Socialist Revolution, which marked the beginning of the general crisis of capitalism, and the building of a socialist society based on genuine equality, dealt a crushing blow at vulgar economic theories, which maintained that incomes had to be and would always be distributed on marginalist principles. Bourgeois theorists now had to work out an economic policy for stabilising capitalism in order to prevent any further revolutionary upheavals and drop-out of more units from its system.

Keynes's theory, considered in detail in the preceding chapters, had played an important role in this respect. Let us take another look at it from the standpoint of the new approach to the redistribution of incomes, taken by vulgar bourgeois economics. Keynes proved that the problem could not be solved at a microeconomic level, that is, by adjusting the "economic agent" to market laws. According to his theory, the crucial role here had to be played by the state, whose task was to combat economic crises and mass unemployment, which gave rise to forms of mass impoverishment that were particularly dangerous in social terms.

According to neo-classical theory, the economy is governed by the market, through which the consumer makes his demands to it; the state does not deal with the consumers, but only does the will of its citizens—the electorate—who make definite demands on it in the matter of meeting social requirements, for which purpose they set aside a share of their incomes in the form of taxes.

In contrast to that theory, Keynes maintained that the state's duty was not only to regulate the economy in order to ensure full employment, but also to make investments that would compensate for the shortfall in private investments in time of crisis. In Keynes's model, the state used the national income to make investments and help the unemployed, something that made it a component of the economic system instead of an external force. On the strength of the Keynesian theory, capitalist apologists asserted that the spontaneous market regulation of the economy was giving way to state regulation, known as statism. Under the influence of the statism concept, they came up with numerous versions of the "welfare state" theory, portraying the state as a supra-class force that takes care of all the members of society.

Statism was the first, embryonic theory of the transformation of capitalist society, which contained only vague allusions to changes in its social structure. These usually boiled down to the sophistic argument that since the electorate determined the makeup of the government, they could influence not only its law-making, but also its economic policy.

The "Keynesian revolution" centred on a modernised version of the bourgeois-reformist concept of the redistribution of incomes, according to which such redistribution had to be carried out by the state at a macroeconomic level. Keynes emphasised, however, that the state's chief function was to ensure capital investments in crisis periods, when declining private investment had to be artificially stimulated. Keynes also wanted to see a certain redistribution of incomes in favour of the poorer strata in order to stimulate capital accumulation. According to his "fundamental psychological law", the propensity to consume declined with an increase in incomes. The propensity to consume is greatest among the poor, and a redistribution of incomes in their favour entails an increase in aggregate demand, which stimulates the growth of production and capital accumulation.

Keynes sharply criticised the wages theory of the well-known British economist A. C. Pigou, who maintained that cuts in workers' wages could help to increase their employment. Keynes said that the decline in employment was due to macroeconomic uniformities, primarily to a shortage of investment and a drop in aggregate demand. Apart from that, Keynes believed that direct wage cuts were socially dangerous, for these would inevitably meet with resolute resistance on the part of the working class. His idea was to reduce wages covertly, imperceptibly for the workers, with the help of "regulated inflation". That method, he believed, made it possible to raise nominal wages while ensuring a reduction in their real content as a result of price inflation, which also helped to boost profits.

At first, the "regulated inflation" proposed by Keynes created the illusion that incomes were going up and led to a decline in the strike struggle, but subsequently these illusions were dispelled by the hard facts. Since the Second World War, inflation has become a major factor in aggravating the contradictions between labour and capital, and this has led to an unprecedented upsurge in the class struggle in the developed capitalist countries.

So, Keynes's theory only recommended new methods for a fairly limited redistribution of incomes that would help to moderate class contradictions, but did not rise to theoretical generalisations that would create an illusion of the social transformation of capitalism.

The postwar neo-Keynesian theories of economic growth were also unable to make much headway in this direction. True, their authors criticised Keynes's theory for its static nature, saying that it dealt solely with anti-crisis and emergency measures in the sphere of incomes redistribution. The dynamic neo-Keynesian theory of growth provided for a constant increase in the working people's incomes as the result of a steady growth in the national income, which, the neo-Keynesians maintained, would lead to an increase in the share of the pie assigned to the working class without any special measures for its redistribution. The growth theory recommends methods for increasing the working people's incomes which (as Chapter One showed in detail) help to contain their class struggle for a radical redistribution of the national product, as endangering the foundations of capitalist society.

The theories of redistribution elaborated by bourgeois economists under the general crisis of capitalism to a certain extent depart from the traditions of the exchange concept. The changes in the sphere of production that are objectively connected with the material preparations of prerequisites for socialism and conditioned by the class struggle are presented as the result of deliberate government policy aimed at humanising capitalist exploitation and realising in capitalist society the so-called equal opportunities principle, enabling every individual to improve his lot without any revolutionary transformations in the economic system. In this instance, bourgeois economists follow in the wake of the real changes in the system of state-monopoly capitalism, using delusive semblances to mystify the reality.

It was already shown above how state intervention in the economy engendered the myth about the state's supra-class role and its urge to create a "welfare state".

Marxists have done much to expose the hypocritical concepts of "workers' participation in running production" which are based on the argument that when a worker buys a few shares he is entitled to take part in shareholders' meetings as an "owner" of the firm. In the theories of "democratisation of capital" and "people's capitalism", which will further be considered in subsequent chapters, hypocritical talk about increasing the working people's incomes is coupled with equally hypocritical talk about raising their social status.

In the past few years, bourgeois economists have sought to substantiate the equalisation of incomes concept with the theory of "human capital", which says that under the scientific and technical revolution the very needs of production enable any worker to rise—spontaneously and without any struggle—to a high material level. The only thing he has to do is to stop "wasting" his free time and money savings on egoistic amusements and use these to acquire an education. Naturally, the theory says nothing about the fact that the "owner" of such "human capital" should look for an owner of the means of production, that is, of real capital, in order to sell him his labour power, which the owner will exploit for the sake of profit.[1]

The logic of the class struggle in individual countries and on the international scene inevitably discredits the apologetic theories of incomes equalisation.

2. Theories of "Industrial Society"

Problems relating to the social transformation of capitalism through changes in its class basis were first formulated by bourgeois economists in the theories of "industrial society". It was the changes in the economic structure of the developed capitalist countries under the impact of the scientific and technical revolution that provided the material prerequisites for the emergence of these theories. Bourgeois economists use them to disprove the Marxist thesis of the decisive role of the working

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[1] For details see Chapter Eleven.

class in present-day capitalist society, and also to prove that its influence has waned for two reasons: first, because its share in the economy is diminishing in view of changes in the economic structure; and second, because in the so-called consumer society the working class acquires consumer durables and so develops into a propertied class, which is concerned about retaining and multiplying its property, into a "middle class", whose relations with the owners of the means of production are no longer antagonistic.

The working class, engendered by the industrial revolution of the 18th and 19th centuries, is the class that has already put an end to the sway of capital in many countries and started the transition from capitalism to socialism on a global scale. In most countries of the world, however, the working class is still oppressed by capital and is used only as an appendage to the machine and a material factor of production.

But the international position of the working class has since then undergone a radical change due to the simultaneous unfolding of the world revolutionary process and the world scientific and technical revolution, the basis for the allround competition between the two antagonistic systems, socialism and capitalism. Ideological struggle is of vast importance in this competition. In the course of this struggle, it is particularly important to study the trends in the scientific and technical revolution from the standpoint of its influence on the future of the working class.

What are the arguments used by bourgeois ideologists to prove that the role of the working class in capitalist society has now declined?

The scientific and technical revolution not only leads to changes in production technology and organisation, but also entails profound economic and social changes in the capitalist society as a whole, primarily in the structure of the working class. The share of material production tends to decrease, and that of the services, education, scientific research, management, and the information service to increase. In the past few decades, the overall number of wage workers in the developed capitalist countries has increased largely owing to the growth in the number of service personnel, office employees and intellectuals.

Employment in material production first showed a tendency to stabilise back in the 1950s, and since the mid-1960s, it has steadily decreased. From 1950 to 1973, the share of those employed in material production in the United States went down from 40.9 per cent to 31.6 per cent, and the figure for the non-production sphere increased from 59.1 per cent to 68.4 per cent.[1] In the developed capitalist countries of Western Europe, service employment increased from 34.5 per cent in 1958 to 40.2 per cent in 1968.[2]

The objective demands of technical progress and broad use of scientific and technical achievements in production tend to reduce the share of manual workers in that sphere as simple labour gives way to more complex, skilled and, consequently, more productive labour, which increasingly resembles that of engineers and technicians. Thus, from 1950 to 1973, the share of manual workers in the total US labour force went down from 39 per cent to 35 per cent (while their total increased from 23 million to 29 million). The growth of skills among those employed in the production and non-production spheres are largely due to an extension of the general education and special training systems.[3]

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[1] See: *Statistical Abstract of the US, 1973*, p. 228.

[2] Russell Lewis, *The New Service Society*, Longman, London, 1973, pp. 3, 164.

[3] From 1950 to 1973, outlays on education in the United States increased from $9 billion to $80 billion, and the average period of education, from 9 to 12.4 years (for details see Chapter Six).

In the past decades, the number of white-collar workers has rapidly increased both in absolute and relative terms. In 1950, there were fewer office workers in the United States than manual workers, and in 1973, there were over 30 per cent more of them than of the latter, and their total came to almost one-half of the labour force. In view of that, bourgeois theorists began to talk of a "white-collar revolution".[1]

Scientists and technicians—an ever more influential social force—have a special place in the category of white-collar workers. They are the fastest growing occupational group. In the past few decades, its size has doubled or more than doubled in most developed capitalist countries. From 1950 to 1973, total employment in the United States increased by 40 per cent, the number of engineers by almost 200 per cent, and the number of employees with a higher and secondary special education went up by 160 per cent, from 4.5 million to 11.6 million.

Those bourgeois economists and sociologists who advocate the theories of "industrial" and "postindustrial" society absolutise the changes in the socio-occupational makeup of the working class and deduce the role of various social groups in the class struggle not from their position within the exploitation system but from their role and place in the technical development of production, seeking to prove that the working class is "disappearing".

But in spite of all the attempts to prove that there is no longer any class struggle under capitalism, the scientific and technical revolution has not diminished the role of the working class. It has only reduced the share of low-skilled manual workers, so changing the structure of the working class, whose numbers have on the whole increased with a simultaneous enlargement of its social boundaries as a result of ever greater class differentiation through-

[1] See: Russell Lewis, *op. cit.*, p. 44.

out the whole of capitalist society. A sizable section of office workers, scientists and technicians are losing their privileges as a social stratum, and the share of the liberal professions among all intellectuals is decreasing. Their social interests, as those of wage workers, are tied in ever closely with those of the working class.[1]

At the same time, the scientific and technical revolution entails a rapid growth of the working-class intelligentsia (adjusters of automatic equipment, electronic computer operators, etc.), something that fully confirms the trend towards the emergence of an "engineering proletariat"[2], a trend noted by Lenin.

Bourgeois theorists ignore the real changes in the class structure of the developed capitalist countries and seek to prove that, far from exacerbating the class antagonism, the uniformities of the scientific and technical revolution help to bring all the social groups closer together, so that the class struggle gradually subsides.

Let us consider the two most popular versions of the bourgeois theory of "industrial society". One of these was formulated by the French sociologist Raymond Aron, and the other, by the US economist John Kenneth Galbraith.

In terms of class substance and purpose, these two theories have more common features than distinctions. But to understand the role each of them plays in the strategy and tactics of the class struggle, and their place in apologetic economics, one should bring out the specific economic and social prerequisites that led to their emergence and development, for the use of this or that apologetic theory largely depends on the political maturity of the working class and its experience of class struggle, and also,

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[1] See: *International Meeting of Communist and Workers' Parties, Moscow, 1969*, Peace and Socialism Publishers. Prague, 1969, p. 25.

[2] See: *Lenin Miscellany XXXVII*, p. 213 (in Russian).

naturally, on the political experience of the bourgeoisie itself and the ideological legacy at its disposal.

Let us begin with Europe, where the most experienced and politically sophisticated contingent of the bourgeoisie confronts a proletariat steeled in class battle and dedicated to the ideals of socialism.

It is hardly surprising that in substantiating his "industrial society" theory, Raymond Aron pointed out that the idea of such a society was first formulated by Saint-Simon. He could not ignore the brilliant founder of one of the most mature theories of critical-utopian socialism, an important landmark in the history of French social thought and in the development of the political consciousness of the working class. But although Aron posed as Saint-Simon's successor, in actual fact he followed in the wake of the latter-day Saint-Simonians, who perverted the founder's revolutionary aspirations for apologetic purposes.

For a deeper insight into the problem, let us recall how Marx and Engels defined the historical place of critical-utopian socialism and communism.

First of all, the architects of utopian socialism were

> "conscious of caring chiefly for the interests of the working class, as being the most suffering class. Only from the point of view of being the most suffering class does the proletariat exist for them."[1]

They did not and could not act as working-class ideologists, both in view of their social status and for the simple reason that the working class itself was still unprepared for independent historical action.

> "They want to improve the condition of every member of society, even that of the most favoured. Hence, they habitually appeal to

[1] Karl Marx and Frederick Engels, *Collected Works*, Vol. 6, p. 515.

society at large, without distinction of class; nay, by preference, to the ruling class... they reject all political, and especially all revolutionary, action; they wish to attain their ends by peaceful means, and endeavour, by small experiments, necessarily doomed to failure, and by the force of example, to pave the way for the new social gospel."[1]

But, as Marx and Engels pointed out, the critical elements in the writings of the great utopians aimed at exposing the foundations of capitalist society provided some "most valuable materials for the enlightenment of the working class".[2]

As the class struggle developed, Saint-Simon's followers, who formed reactionary sects, did their utmost to blunt that critical edge, consistently endeavouring to "deaden the class struggle and to reconcile the class antagonisms".[3]

Methodologically, Aron's concept derives from the theory of Auguste Comte, one of Saint-Simon's followers who distorted his ideas, disavowed his behests and did everything to help like-minded bourgeois sociologists to blunt the class struggle.

Engels wrote: "Comte took all his bright ideas from Saint-Simon."[4] But in spite of this fact, which created the false impression that it was Comte himself who formulated daring ideas and had brilliant insights, his positivist philosophy, to quote Engels, was "a narrow, philistine way of thinking".[5]

We note this point because Comte's positivism provides the methodological basis for present-day concepts of "industrial society" which are being widely used to substantiate the social transformation of capitalism.

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[1] *Ibid.*

[2] *Ibid.*, p. 516.

[3] *Ibid.*

[4] Karl Marx and Frederick Engels, *Selected Correspondence*, Progress Publishers, Moscow, 1975, p. 453.

[5] *Ibid.*

If one is to separate Saint-Simon's theory from that of Comte, who distorted the great utopian's brilliant ideas, one should find out how Saint-Simon, the true author of the "industrial society" concept, came to formulate that concept.

Saint-Simon, who regarded himself as Rousseau's follower and shared his ideas about freedom and equality, believed, in contrast to his teacher, that mankind's Golden Age was still to come. He believed that it would arrive with the development of science and technology, and also with the revolutionary transformation of society. In spite of the fact that during the Jacobin dictatorship Saint-Simon was imprisoned and narrowly escaped being guillotined, he recognised the revolution as a natural and inevitable stage in society's development, without which there could be no new stage of evolutionary development. He saw mankind's history as an evolutionary process interrupted by revolutions.

But in analysing the results of the victorious bourgeois revolutions in Britain and France, Saint-Simon saw that the hopes he had pinned on industrial development were not realised. The capitalist system only widened the gulf between the rich and the poor. The people's lot was now even worse than it had been under the old system, for vast masses of peasants, handicraftsmen and small tradesmen, ruined by capitalist competition, fell victim to poverty and unemployment. He was disappointed with the teaching of Adam Smith, who had predicted, on the basis of man's "natural law", capitalist society's steady progress towards the "wealth of nations". Nor could Saint-Simon accept Ricardo's arguments about the "natural" causes of low wages, which stemmed from Malthus's doctrine that poverty was inevitable. Saint-Simon tried to answer the questions posed by historical reality by analysing the uniformities of the French revolution with brilliant foresight. In that context Engels wrote:

> "...to recognise the French Revolution as a class war ... between nobility, bourgeoisie, and the non-possessors, was, in the year 1802, a most pregnant discovery".[1]

Saint-Simon drew the conclusion that the revolution was carried out by the masses, but was directed by "metaphysicians and jurists". Their criticism was powerful, but they were unable to create anything positive. They thought about the forms of power but what one had to think about was the essence of life, the ways to develop production. He urged all scientists to work for a new and positive epoch, when empty talk about freedom would give way to industrialism, and the critical and revolutionary philosophy of the 18th century, to a philosophy of organisers and creators. He believed that the "industrials" were the most important social stratum. Among these he ranked entrepreneurs and organisers of production, engineers, mechanics and workers, and also bankers, architects, writers, and artists, that is, all those who were engaged in what he believed to be useful work. On the other hand, there were the idlers living at society's expense: the gentry, the coupon-clipping bourgeois, and also pseudo-scientists, jurists and metaphysicians. There should be no parasites in society, everyone should work. All power should pass into the hands of the "industrials", because industry, integrated with the help of banks, was to become the most powerful force in the state. But that great revolution had to be effected from above. The fundamental distinction of the new industrial system would be man's domination of things, in contrast to the old system, where man dominated man. Production was to be based on planning and was to be run from a single

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[1] Frederick Engels, *Anti-Dühring*, Progress Publishers, Moscow, 1977, p. 313.

centre. In his final work, *New Christianity*, Saint-Simon singled out the working class from among the industrials and wrote that society's major task was to improve the moral and physical condition of the poorest and most numerous class as quickly as possible. That, he believed, was the only "divine element" in the Christian religion.

Saint-Simon died in 1825, and in 1831 the silk-weavers of Lyon staged an uprising and for ten days held power in the city. Terrified by the spectre of revolution, Saint-Simon's followers purged his teaching on industrial society of everything that showed his sympathy for the working class or substantiated socialist ideas, and used it as a basis for Positivism, a philosophy that was harmless for the bourgeoisie.

In 1842, August Comte put out his *Course of Positive Philosophy*, and in 1854, a four-volume *System of Positive Policy*, laying the foundations of Positivism, which is the main source of the ideas behind present-day "industrial society" concepts.

Comte believed that social history reflected the categories of thinking that determined the nature of its ruling elite. According to his theory, mankind went through three stages of development: the theological, when all phenomena were explained by the divine will and power was in the hands of the clergy; the metaphysical, when mankind thought in abstract categories and was run by law-makers and lawyers; and the positive, when the exact sciences appeared and their development called for the power of industrialists and scientists.

In his "hierarchy of sciences", the natural sciences were followed by only one social science, sociology, which he called social physics. It was divided into two sections: social statics and social dynamics. Social statics was based on the law of order embodied in such social institutions as the family, groups of citizens and the state. Social dynamics derived from the mental process.

The order based on the statics of the existing social institutions and the progress caused by the development of science guaranteed class harmony in a "positive society".

The latest theories of "industrial society" strictly conform to that postulate, combining the statics of the social institution of private property in the means of production with the dynamics of production connected with the scientific and technical revolution. But since it is no longer possible openly to defend capitalism and present it as the ultimate form of social development, without taking into account the social system that confronts it, Raymond Aron, for instance, has put forward an idea about the "pluralism" of world development, which means the existence of different types of industrial societies on the basis of historically rooted social structures.

Explaining why he has abandoned the word "capitalism", Aron says: "Instead of capitalism I have chosen industrial society ... as the principal concept." Such a society, he believes, can be spelt out as a "technical, scientific or rationalised society",[1] a society dominated by large-scale industry, which can be owned either by the state (like Renault in France) or by joint-stock companies (like Citroën).

Aron said that such a society, which recognises all forms of property, has

> "three main forms of social differentiation: through the division of labour, through the hierarchy of wealth, power and prestige, and through the plurality of groups which are formed and come into conflict with each other within the society as a whole."[2]

So, in a "pluralist society" there is no class struggle, but only conflicts between social groups (strata).

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[1] Raymond Aron, *18 Lectures on Industrial Society*, Weidenfeld and Nicolson, London, 1968, p. 235.

[2] *Ibid.*, p. 232.

Such were Aron's views on "industrial society" in the early 1960s, when he still believed that capitalism could be stabilised on the basis of the scientific and technical revolution, which, he thought, ensured economic growth, while helping to maintain the social structures in a state of steady equilibrium. But in the second half of the 1960s, when the class contradictions sharpened and the general crisis of capitalism deepened, Aron had to alter his views on the prospects before "industrial society" and put out a book entitled *Progress and Disillusion. The Dialectics of Modern Society.*[1]

Aron's disillusion in progress springs from his fear of communist influence in those West European countries where the Communists are supported by broad social sections and have an influence among the intelligentsia. Aron warns the intelligentsia about the dangers of flirting with Marxism, and tries to scare it with the prospect of a despotic dictatorship which, he says, could result from a victory of communist ideas. At the same time, he seeks to inspire the intelligentsia with faith in capitalism, and to prove that by transforming the social structure of the developed capitalist countries "industrial society" obviates the laws of class struggle envisaged by Marxism. Aron calls for a repudiation of the belief that it is possible to realise these major ideals —equality, freedom, allround development of the individual, and mankind's unity, which the Marxists use to inveigle the simple-minded. If the ideological struggle against communism is to be successful, it is also necessary, he believes, to dispel some of the bourgeois-reformist illusions, which he accepted to some extent in his early views on "industrial society".

First of all, he seeks to discard the illusions of equality and equal opportunities spread by the

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[1] See: Raymond Aron, *Progress and Disillusion. The Dialectics of Modern Society*, Frederick A. Praeger Publishers, New York, 1968.

ideologists of bourgeois reformism, who saw the striving for equality as the ideological basis of the class struggle against the bourgeoisie. He argued that the real contradictions in the developed capitalist countries are no longer determined by the struggle between the two main classes, but by a more complex system of social stratification, which has emerged with the disappearance of these classes and of the inherent interrelationships between them.

Aron writes that social evolution is moving

> "toward less heterogeneity between one stratum and another, hence toward less homogeneity within each stratum; toward less inequality in education, hence toward a greater degree of ascending social mobility; toward less solidarity within the strata...,"[1]

that is, he implies a tendency to a damping down of social conflict.

Aron aims to prove that social mobility and opportunity for advancement destroy the "myth of collectivism", for they help to form a ruling elite in "industrial society" into which anyone can make his way. And the unavoidable conflicts between and within the strata that are caused by the social mobility only serve to stabilise "industrial society", making it immune to revolution.

Posing as an objective critic of the shortcomings of both systems, Aron concludes that their coexistence is inevitable, for the change of formations predicted by Marxism on the strength of the laws of the class struggle has allegedly turned out to be a myth, while pluralism in social development is a fact.

Aron's disillusion with progress also manifests itself in his loss of faith in democracy with its ideal of equal opportunities. He calls on Western

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[1] R. Aron, *op. cit.*, p. 11.

intellectuals to give up that illusion, for "the iron law of oligarchy and the changing demands of technology do not permit them completely to realise their ideal of self-government or of equality of opportunity or rank".[1] Although the masses' educational level has been rising and "the minority capable of rational discussion grows larger, ... the gap between this minority and the rest of society is not becoming narrower".[2]

The Marxist idea of the allround development of the individual, Aron believes, is also unfeasible in "industrial society", for it clashes with the very "culture of the industrial civilisation". Its realisation does not depend on the prevailing form of property or on policy.

Aron says:

> "All societies... continue to train the *men they need* but ... none, despite its proclaimed objectives, needs to have all men realize fully their individual potentialities. No society *needs* to have many men become personalities fully capable of freedom in relation to their environment."[3]

In contrast to Marx, who explains the individual's alienation under capitalism by exploitation, which makes it impossible for the wage worker to dispose of the results of his own labour and take part in running production, Aron describes alienation as "the price to be paid for the conquests of the civilisation itself".[4]

Aron believes that alienation is rooted in the insoluble contradictions between the individual and the role he performs, for any form of socialisation (in family life, production and politics) that gears his activity to a common goal suppresses the individual, his instincts and natural urges for the

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[1] R. Aron, *op. cit.*, p. 39.
[2] *Ibid.*, p. 41.
[3] *Ibid.*, p. 106.
[4] *Ibid.*, p. 126.

sake of the role assigned to him, so that his alienation is inevitable.

In this way, Aron seeks to disprove the great internationalist Marxist idea about the oneness of mankind, which can consciously control the laws of social development on the basis of common goals. In the first and second parts of his book, entitled "Dialectics of Equality", and "Dialectics of Socialisation", Aron tries to refute the Marxist ideas of equality and to prove that they can never unite for the purpose of achieving common goals, and in the third part, "Dialectics of Universality", he argues that there can never be any friendship among the nations on this planet.

In his opinion, the scientific and technical revolution, running against the background of the struggle of "politico-economic ideologies", serves to strengthen nationalism, and nationalism is bound to triumph over the laws of class struggle. This argument is spearheaded against the Marxist-Leninist doctrine, which says that proletarian internationalism provides the basis for friendship and cooperation among all the peoples of the world.

Aron believes that "industrial societies" can never have a common goal, for each of these has its own system of values. Ultimately, he draws the conclusion that it is impossible to predict the shape of the society to come.

Aron's refusal to prognosticate the future, his apologetics of capitalism and, at the same time, the fact that he cannot deny the viability of socialism, which has created its own type of "industrial society", are characteristic of the bourgeois ideologist who has to bear in mind that in his own country, as in other West European countries, socialist ideals are a source of inspiration for many working people.

In contrast to Aron, who considers social institutions outside the context of economics, J. K. Galbraith regards these as components of the latter, maintaining that the social transformation of capitalism does not result from society's growing social mobility, but from changes in production, where the big corporation has come to play the decisive role. Social stability in an economically dynamic society is due to interaction among such institutions as the corporations, the trade unions and the state. It is these institutions rather than the market with its competition that make up the foundation of the corporate system that predominates in the US economy.

Galbraith gives a different recipe for the social transformation of capitalism within the framework of "an industrial society" not only because he starts from positivist postulates, interpreting it as an economist who relies on bourgeois economic dogmas. The important point here is that the class struggle in the United States is not as intensive as it is in Western Europe. The US working people have yet to rally together for a mass movement against monopoly rule. At present, the AFL-CIO is headed by reactionary, anti-Communist leaders. In these conditions, it is only natural that a US economist should maintain that the monopolies, which enjoy the support of reactionary trade union leaders, are the social institution that has the potentialities for a social transformation of capitalism. His apologetic concept hinges on the problem of achieving a "social balance" by establishing new proportions between personal consumption and the public services, like transport, education, health care, etc.

But Galbraith also has to take into account the changing situation in the world, and his views, like those of Aron, have gradually evolved.

In his book, *The New Industrial State*,[1] where he spells out his ideas on the social transformation of capitalism, Galbraith says that the imperatives of

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[1] See: John Kenneth Galbraith, *The New Industrial State*, Houghton Mifflin Company, Boston, 1967.

technological advance make it necessary for the bigger US corporations to plan their economic growth over the long term, ignoring the principles of profit maximisation. He draws the conclusion that economic power in the United States now belongs to what he calls mature corporations run by managers who shun the capitalist mentality. They plan production, seeking to obtain optimal profit, which allegedly takes into account both the long-term interests of the stockholders and those of the workers: the stockholders enjoy a guaranteed income, and the workers, relatively high wages. So, Galbraith regards the mature corporations as the social institutions that eliminate the class conflict between capital and labour, which endangers the existence of capitalism.

In his next book, *Economics and the Public Purpose*,[1] Galbraith continues his analysis of the corporation's role as an institution that brings about the social transformation of capitalism.

He maintains that owing to technological advance, which has made the planning of supply and marketing, as well as that of production, with the use of powerful data-processing systems and methods of systems analysis, a necessary component of management, there has been a qualitative change in the mechanism of economic decision-making within the big corporations. In view of the gigantic flows of information, the right to take decisions is now in the hands not only of the top functionaries who are in charge of the system as a whole, but also of those who run the subsystems of the complex, multisectoral corporation. Galbraith calls this new social stratum the "technostructure". The title itself implies that this stratum has been engendered by the STR.

Galbraith's technostructure includes not only those who organise and run the technological pro-

[1] See: John Kenneth Galbraith, *Economics and the Public Purpose*, Houghton Mifflin Company, Boston, 1973.

cess, but also all those who ensure the influence of the corporation on the external environment: a complex of sales, advertising and marketing men; of public relations experts, lobbyists, lawyers and men with a specialised knowledge of the Washington bureaucracy and its manipulation. He emphasises that "not any single individual" but the technostructure as a whole becomes the "commanding power" in the corporation.

He maintains that the big corporation in effect operates without the participation of the owners of capital, for the whole power of decision-making has passed from the shareholder to the technostructure.

This produces the illusion that the owners of monopoly capital have voluntarily withdrawn from decision-making in the corporation, and are well satisfied to clip coupons.

At the same time, Galbraith emphasises that the technostructure of the big corporation is closely tied in with the state. As a client of the big firms, the state has set up its own subsystems of economic management, through which it maintains long-term contractual relations with these firms, so that the state bureaucracy coalesces with the corporate technostructure. The state promotes the interests of the big firms and is least concerned about the industries which are not dominated by these firms. This "bureaucratic symbiosis" between the state and the big corporations harms the sectors of the economy where the latter are not in control.

Galbraith calls the corporation-dominated part of the economy the "planning system", and all its other units, the "market system". He says that a shortcoming of the "planning system" is that the one thousand giant corporations within it, which produce approximately half of all the goods and services not provided by the state, slow down the development of the market system, which includes about 12 million small firms, in those sectors of the economy where competition reigns supreme. He deplores the defects of such planning, but does not censure the corporations, which he sees as the motive force of progress.

In contrast to the Marxist theory, Galbraith spins out a myth about the disappearance of traditional classes and regards social antagonisms only as contradictions between the two "systems" in the US economy. Thus, the "planning system" exploits the "market system", where there are no powerful trade unions and where the workers receive lower wages or have relatively longer working hours. To survive in the competitive struggle and obtain the necessary income, the small entrepreneur has to resort to "self-exploitation".

Galbraith's model of the market system is an abstraction and is out of touch with reality. In the United States, where class differentiation is very marked, there is no socially homogeneous market system. The exploited and "self-exploiting" small firms do not hold the commanding heights even in agriculture, retail trade and the services, to say nothing of industry, where they play an insignificant role. The bulk of these small firms in all the sectors of the economy is within the sphere of influence of the big corporations, which find it more profitable to deal with specialised enterprises willing to face the hazards of competition than to set up their own enterprises producing small-batch products or catering for small local markets.

Within the market system, there are sharp class contradictions between the exploiters and the exploited. The social structure of that section of society which Galbraith refers to the market system is not only heterogeneous in class terms, but is also dynamic, tending to become even more heterogeneous. This is also due to the close interrelationship between the monopoly and the non-monopoly sectors of the US economy.

In reality, a sizable section of the market system is not opposed to the technostructure, but to the sway of monopoly capital, which controls not only the planning system, but also a large part of the market system. That is why within the market system there are potential anti-monopoly forces unnoticed by Galbraith: the working people, who are coming to realise that their hardships are due not only to their immediate exploiters—the owners of small and medium enterprises—but also to the monopolies, which have a stake in preserving zones of poverty and backwardness. With the help of small businessmen and their firms, the large corporations, which have included them in their economic empires, subject a sizable part of their country's population to ruthless oppression and social discrimination. But the small businessmen themselves often regard the powerful trade unions, and not the monopolies as their chief enemies, which "corrupt" the workers with high wage demands and social insurance. Small business, operating under market competition, which does not yield monopoly profit, cannot extend such benefits to its workers. Most of them are not members of any trade union and do not conclude collective-bargaining agreements which provide for a guaranteed wage, holidays, etc. That is why state-monopoly capitalism seeks to preserve small business as a social prop and to use it in the struggle against the working class.

Rejecting the Marxist method of class analysis, Galbraith looks for ways of reorganising the market system outside the historically inevitable struggle between labour and capital. Realising that the big firms—the core of the planning system—are incapable of "inter-industry coordination" that would ensure the development of the lagging industries on which the rise in the "quality of life" depends, Galbraith pins his hopes on coordination with the help of reforms from above. It is not the corporations, which are immune to the threat of socialism, but the market system, which is a source of social upheavals, that should be the main target of such reforms.

Galbraith has, in effect, been unable to disprove the Marxist thesis that production for the sake of profit is the one and only purpose of the large corporation.

His argument that the planning system has emancipated itself from market relations is equally unfounded, for sales and purchases on the basis of long-term contracts do not mean that market relations have been eliminated. Moreover, the production ties of the large corporations are much wider.

In actual fact, Galbraith's "planning system" is a monopoly market mediated by state-monopoly regulation, which is based on market laws rather than on nationwide planning.

Banks, investment trusts and the stock exchange are an arena of competitive struggle for more profitable investment of capital. The conditions for victory in that struggle are prepared within the corporations themselves and depend on their ability to diversify their products by setting up new enterprises or taking over existing firms. Competition among the large corporations has nothing to do with genuine planning.

Galbraith seeks to prove that there is no need to change the form of property in the large US corporations, for these automatically free themselves from the power of capitalists and pass into the hands of the technostructure. In these corporations, he says, there is no exploitation, so that "socialism" in the United States (by which Galbraith implies state intervention in the economy) is necessary not for the corporation-dominated "planning system", but for the market system. The latter should be reorganised not on the basis of "doctrinaire socialism" (meaning scientific socialism), which he denounces as deriving solely from ideology, but on the basis of "pragmatic socialism" dictated by the force of circumstances, while the circumstances leading to socialism, he points out, are imperative only in the weakest sectors of the economy.[1]

Among the lagging industries he includes those that cater for the requirements of the least well-off sections of the population: housing, transport and health care. In the United States, these industries can be reorganised only when "socialism is seen as a necessary and wholly *normal* feature of the system".[2] To do this, the United States has merely to take into account the experience of Western Europe and Japan, where this view has allegedly already been asserted.

Galbraith believes that there is no need to convert the large corporations to state property, with the only exception of the military-industrial complex. The technostructure of the large weapons firms is in peculiarly close relationship with the state bureaucracy and each of these draws power from its support by the other. He believes that the combined power of the two bureaucracies would be usefully reduced by converting the large specialised weapons firms into state property.

But everything depends on the nature of such state property. A significant point to note is that in calling for the nationalisation of the weapons firms, Galbraith seeks to protect their owners. He wants the government to acquire their stock at prevailing stock-market valuations. He writes:

> "For unduly weak industries and unduly strong ones—as a remedy for an area of gross underdevelopment and as a control on gross overdevelopment—the word socialism is one we can no longer suppress. The socialism already exists."[3]

In effect, Galbraith's "socialism" does not go beyond the principles of a "mixed economy" func-

[1] See: John Kenneth Galbraith, *op. cit.*, p. 279.
[2] *Ibid.*, p. 280.
[3] *Ibid.*, p. 285.

tioning on the basis of state-monopoly capitalism. But in spite of that, some ideologists of Big Business have accused Galbraith of just about siding with Marxism.

Why is that so?

The point is that in a number of developed capitalist countries, where there is a powerful left-wing front aiming at more democratic management of state enterprises and democratic nationalisation that would pave the way for the country's movement towards socialism, monopoly capital seeks to reprivatise the state sector in order to strengthen the power of the corporations. Only recently, one of the arguments in favour of this was drawn from Galbraith's earlier book, *The New Industrial State*, where he tried to prove that the "mature corporations" ensure rapid growth rates and higher earnings for its workers and employees. But later on, in his *Economics and the Public Purpose*, Galbraith was no longer enthusiastic about the virtues of all the large corporations. He admitted that their constant urge to expand and to raise prices was a source of uncontrolled inflation and economic instability.

Moreover, he denied the need for rapid economic growth, emphasising the social aspects of the "quality of life" problem and environmental protection. Meanwhile, in the conditions of intensifying struggle for marketing outlets, high growth rates are of paramount importance for monopoly capital in many countries.

Nor can Big Business approve of Galbraith's programme for tax reforms. He says that the high incomes of the more affluent strata should be reduced, and that the way to harmonise the US economic development is to increase the incomes of the poorer strata. To achieve this, he proposes not only progressive taxation, but also an increase in the minimum wages of non-unionised labour. He calls for encouragement of union organisation in small business, the services and agriculture. In proposing wage and price controls as a permanent or long-term measure, he emphasises the need to use these not to perpetuate the existing distributive relations, but to promote greater equality of income.

One point here remains to be cleared up: which forces are capable of achieving the goals set by Galbraith?

According to his concept, the US economy itself has no immanent laws working towards these goals.

But, wittingly or not, his facts merely illustrate the operation of the basic economic law of capitalism—the law of surplus value—which in itself rules out the possibility of equalising the incomes of the exploiters and the exploited. It is the ruling class, which owns the means of production, that determines and realises the goals of US economic policy. The law of surplus value inevitably gives rise to antagonistic contradictions in the sphere of distribution, which can be resolved only through class struggle.

In the United States, where the economy is completely dominated by monopoly capital, goals opposite to those being realised by its ruling party can be formulated only by a party voicing the interests of the working class. Under the historically evolved two-party system in the United States, no bourgeois party regards the word "socialism" as "respectable". Galbraith notes the shortcomings of the existing two-party system. He may even regret that there is no party in the United States prepared to adopt his programme for a "new socialism", which has long been accepted in West European countries. But since there is no such party in the United States, he pins his hopes on a renewal of the Democratic Party.

The fact that a leading US economist calls for acceptance of the word "socialism" and advocates some objectively progressive reforms is a clear indication not only of the crisis of bourgeois economics, but also of a shift to the left against the background of a further deepening of the general crisis of capitalism. Bourgeois theorists are evidently no longer in a position to prove that US capitalism is "exceptional" and that the laws of revolutionary development discovered by Marxism do not apply to it. One indirect proof of this is the "industrial society" doctrine, which Galbraith has modernised by supplementing it with the idea of "pragmatic socialism" and urging the US ruling class to learn from Western Europe.

The two most popular versions of the "industrial society" doctrine considered above do not fit into the framework of traditional vulgar economics, which regards itself as a science about the optimal use of limited resources. Both versions are an attempt to synthesise bourgeois economics and sociology into a new apologetic doctrine to refute the Marxist theory of class struggle and replace it with a bourgeois-reformist myth about the elimination of capitalist society's class antagonisms on the basis of the scientific and technical revolution. Instead of analysing the productive forces and relations of production, the exponents of the "industrial society" doctrine concentrate on technological advance, in effect, leaving out society's chief productive force, man himself, with the whole system of production relations that determine his being and consciousness. The individual's behaviour and the decisions he adopts are interpreted only from the angle of his subjective psychology and the social psychology of the various strata, that is, social groups and sections substituting for classes. In these theories, social stratification considered outside the context of production relations takes the place of division into classes.

"Industrial society" concepts are closely tied in with bourgeois-reformist concepts of the gradual equalisation of incomes, which lie at the root of theories of economic growth, including its highest stage, which the US bourgeois economist Walt Rostow calls the mass consumer society.[1]

Without going into the details of that bourgeois-reformist concept, let me emphasise its interconnection with the doctrines considered above in order to bring out the bourgeois substance of the social stratification on which "industrial society" doctrines are based.

Under these doctrines, bourgeois law is to be perpetuated. Industrial society is an authoritarian system run by a social elite, which Aron sees as an oligarchy of the leading firms, and Galbraith, as the technostructure of the large corporations. Both imply a concentration of power in the hands of Big Business.

"Industrial society" doctrines do not provide for any solution of global problems. Thus, Aron's "pluralist world" leaves mankind no hope of a bright future, and Galbraith believes that it is up to the multinational corporations—the core of the US "planning system"—to put the world economy in order.

Naturally, no theory of the social transformation of capitalism based on the continued sway of Big Business can meet the democratic aspirations of the working masses, whose frame of mind is increasingly anti-imperialist and anti-monopoly. So, alongside the doctrine of "industrial society", bourgeois economists have now adopted the theory of "post-industrial society", which has gained wide currency as a new instrument of bourgeois apologetics. Its distinction is that it denies inevitable rule by Big Business in the society of the future. Such a conclusion is drawn from a mystified interpretation of the real changes in the production structure, where, the advocates of post-industrialism believe, society's centre of gravity has shifted from

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[1] Walt Rostow, *The Stages of Economic Growth. A Non-Communist Manifesto*. Cambridge University Press, Cambridge (Mass.), 1960.

the production to the non-production sphere, so that the decisive role in the ruling elite will pass from businessmen to scientists.

3. Theory of "Post-Industrial Society"

This theory—a derivative of the postulates of "industrial society"—has an important place in present-day bourgeois economics and in the programmes for the long-term regulation of the developed capitalist economy. Why?

"Industrial society" doctrines, as I said above, are pivoted on the social transformation of capitalism based on a misinterpretation of the structural changes in the economy. These doctrines deal with structural changes which have actually taken place and which can be statistically assessed and evaluated in qualitative terms. Different problems arose where economists got down to forecasting economic development until the year 2000, in order to guide the large corporations in their investment strategy with a view to the trends and prospects of the STR. Sociologists also joined in this research, supplementing economic forecasts with models of social development which contrasted with those elaborated on the basis of the Marxist-Leninist theory and the long-term plans of the socialist countries.

The new doctrine was founded by Daniel Bell, Professor of Sociology at Harvard University and Chairman of the Commission on the Year 2000 of the American Academy of Arts and Sciences. In the late 1950s, he began vigorously advocating the doctrine of "post-industrial society" as a weapon in the struggle against Marxism. He organised international symposia and invited representatives of the socialist countries to take part in the "dialogue", emphasising his recognition of the need for the coexistence of the two systems and, at the same time, his hope for an "erosion" of socialism and a convergence of the two systems.

At a symposium in Zurich in the summer of 1970, Bell spelled out the "post-industrial society" theory, its ideological origins and methodological basis.[1] He maintained that sociology had always been marked by an urge to forecast the society of the future and to specify the class that is to play the main role in this society. Among the founders of sociology he named Saint-Simon, Comte, Marx, Weber and Veblen. True, he recognised that Marx's teaching had exerted the decisive influence on the development of 20th-century sociology, for all sociological theories on the prospects of capitalist development were a "dialogue with Marx". He thought it impossible to by-pass or ignore Marx's theory, and so declared: "We have all become post-Marxists."[2]

Bell tried to refute Marxism with the help of a new version of contradictions he had detected between the first and third volumes of *Capital*, which, he says, contained "two different schemes of social development". The first was set forth in Volume One, in the section entitled "The Historical Tendency of Capitalist Accumulation", where Marx proved that capitalism will inevitably give way to socialism. According to Bell, that scheme of "pure capitalism" ... "was a theoretical simplification", for in contrasting the proletariat with the capitalists Marx had allegedly maintained that under capitalism all intermediate strata are bound to disappear. In Bell's view, the second scheme—a scheme of concrete capitalism set forth in Volume Three of *Capital* and allegedly refuting the first scheme—was confirmed by Western historical development. The accumulation of capital through investments by

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[1] Daniel Bell, "The Post-Industrial Society. The Evolution of an Idea". In: *Survey*, No. 2 (79), Spring 1971, London, 1971.

[2] *Ibid.*, p. 107.

banks and by the large corporations connected with them had led to the emergence of a new middle class (managers, technical employees, white-collar workers), which had become the bulwark of capitalism and its evolutionary transformation into a "post-industrial society".

Moreover, Bell maintained, history had not confirmed the conclusion formulated in Volume One of *Capital* about the tendency of the rate of profit to fall, for "the state has been able to intervene and soften, if not prevent, economic crises", and "technology has been an open frontier for the reinvestment of capital".[1] In characterising Volume Three of *Capital*, Bell utterly ignored its Chapter 15, which shows the counter-tendencies to the tendency of the rate of profit to fall, and which brings out the factors that aggravate capitalism's contradictions that lead it to ruin.

Acting objectively as apologist for capitalism, Bell naturally does not mention how Lenin, relying on the conclusions of Volumes One and Three of *Capital*, developed his own theory of imperialism and the general crisis of capitalism and how on that basis there arose the Marxist-Leninist theory of the world revolutionary process, which has been borne out by present-day historical development.

Bell believes that Marx's second scheme was most correctly interpreted by Sombart and Schumpeter.[2] According to Bell, these two apologists of capitalism differ from Marx only in their conclusion that capitalism, in spite of its decline, will not give way to socialism, for the monopoly-based bureaucracy is much too powerful.

But the strongest arguments against Marx, in Bell's opinion, were formulated by Max Weber.

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[1] *Ibid.*, pp. 110-113.

[2] See: Werner Sombart, *Der moderne Kapitalismus*, Vols. I-III, Duncker & Humblot, Munich, 1924-1927; Joseph Schumpeter, *Capitalism, Socialism and Democracy*, Harper & Brothers, New York, 1942.

In his "post-industrial society" theory, Bell uses Weber's "law of general rationalisation", which also says that capitalism will give way not to socialism but to complete bureaucratisation.

Among "industrial society" theorists, Bell prefers Raymond Aron, for the latter devotes special attention to problems of social stratification.

Bell believes that all "industrial society" theorists (among whom he includes Marx) make the mistake of regarding the industrial enterprise, with the social relations taking shape on the basis of machine production, as the main social institution; moreover, all these theorists, he says, take a simplified view of the technocracy, confusing the expert whose function is related to knowledge, and the technocrat, whose function is related to power and politics. Meanwhile, the basic problem of "post-industrial society", as Bell sees it, is to organise science, for the state's power at that stage is determined by its scientific, rather than its industrial potential.

The politico-economic views underlying Bell's concept are most fully expounded in his book, *The Coming of Post-Industrial Society*,[1] which summarises all his research.

According to Bell, one shortcoming of the Marxist-Leninist theory of formations is that

> "the terms feudalism, capitalism, and socialism are a sequence of conceptual schemes in the Marxist framework, along the axis of property relations".[2]

He says that such an axis is no longer relevant to capitalism, for "*ownership is simply a legal fiction*".[3] The vulgar interpretation of property as the owner-

[1] Daniel Bell, *The Coming of Post-Industrial Society. A Venture in Social Forecasting*, Basic Books, Inc. Publishers, New York, 1973.

[2] *Ibid.*, p. 11.

[3] *Ibid.*, p. 294.

ship of things, which Bell attributes to Marxism, is used to pervert the latter out of all recognition. In Marxist political economy, property is not seen as a juridical, but as an economic concept, and provides the basis for production relations, which are the form of development of the productive forces. Formations succeed one another because at a definite stage the form that once ensured the development of the productive forces begins to act as a drag, so necessitating a social revolution which establishes not only a new form of property, but also the rule of a new class.

Having perverted the concept of property in Marxist political economy, Bell goes on to prove that present-day capitalism can avoid a social revolution, for in place of it there has already occurred a scientific and technical revolution, which has raised "industrial society's" productive forces to the highest stage of development. In the transition to "post-industrial society", the material productive forces no longer play the decisive role, for the main emphasis has now shifted to the social institutions responsible for organising theoretical knowledge.

Bell objected to the monistic approach in analysing the uniformities of social development, which is determined, according to the Marxist theory, by the dialectical interrelationship of the productive forces, the basis and the superstructure. He maintained that the social structure (economy, technology) and culture are "ruled by a different axial principle".[1]

Under this eclectic, "multifactor" approach, the form of property cannot serve as a criterion of the fundamental distinctions between the two contending social systems. Bell believes that the Soviet Union and the United States are alike as industrial societies, and the imperatives of the STR are leading them towards convergence into "some new

[1] *Ibid.*, p. 477.

kind of centralised-decentralised market-planning system".[1]

According to Bell, the axial structures of the nascent "post-industrial society" do not relate to the economy, but to the use of theoretical knowledge as society's strategic resource. The basic elements of these structures are the universities, scientific institutions and research organisations, where theoretical knowledge is accumulated, systematised and enriched. The social relations of "post-industrial society" are centred in these structures, and not at the enterprises or in the firms. He says that alongside the "military-industrial complex", a "scientific-administrative complex" has already taken shape in the United States as a new power centre with "undue concentration of influence".[2]

According to Bell, science is detached from the economy and becomes the commanding force. But, in spite of what Bell says, the conversion of science into a direct productive force, as predicted by Marx, does not isolate it from the economy. In the United States, more than in any other capitalist country, science remains under the control of the large corporations and financial groups.

Bell's scheme only reflects in a mystified form some trends in present-day state-monopoly capitalism. Theoretical research in the United States is indeed largely concentrated in so-called non-profit institutions, that is, those directly or indirectly financed by the state. Bell regards the state, which now mostly finances and organises basic theoretical research, as the force that will help to transfer society's resources from commodity-producing sectors to sectors that meet the social requirements in science, education, health services and culture. But this is a source of conflict: who is to wield state power in the "post-industrial society"?

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[1] Daniel Bell, *op. cit.*, p. 348.
[2] *Ibid.*, p. 246.

Under Bell's scheme, this power should be concentrated in the hands of the scientists. But in actual fact the whole party and political mechanism in the countries of state-monopoly capitalism and the corporate structure ensure the rule of politicians who are most closely linked with Big Business. Bell has no alternative but to declare that policy-making decisions in "post-industrial society" will be made by experts connected with the function of knowledge rather than by technocrats connected with the function of the power of corporations and the state. However, he cannot muster any facts to confirm the existence of such a trend.

While seeking to prove the disappearance of classes as a result of social stratification and the concentration of decision-making in the hands of the professionals, Bell cannot promise that the "post-industrial society" will develop without conflict. The whole of that society and all its subsystems are run by an elite. Bell writes:

> "If the struggle between capitalist and worker, in the locus of the factory, was the hallmark of industrial society, the clash between the professional and the populace, in the organisation and in the community, is the hallmark of conflict in the post-industrial society."[1]

In contrast to Galbraith, who calls decision-making specialists "the technostructure", Bell calls them the "meritocracy", that is, an elite consisting of gifted individuals who come from all social strata. He maintains that the populace with its everyday notions can never rise to the level of the elite's scientific knowledge or its understanding of society's real goals.

Nor can Bell offer a coherent solution for the problem of equality in the "post-industrial society".

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[1] *Ibid.*, p. 129.

"Meritocrats" rise on the basis of the "liberal theory of equality of opportunity and of Jefferson's belief in the 'natural aristoi' against the ascriptive nobility".[1] Instead of the so-called principle of equal opportunity, which under capitalism implies glaring inequality of income distribution, against which the masses have been fighting, Bell suggests the principle of "equality of result" for all, which means that talent should be seen as a social asset and that the fruits of its activity should be within the reach of all, especially of the "least fortunate".

As we see, Bell's innovation in this instance does not go beyond the principles of bourgeois charity. But why, then, all the fuss, the elaboration of the theory of the "post-industrial society"?

Bourgeois theorists realise that it is no longer possible utterly to ignore Marxism and that the best way to fight it is to borrow some of the Marxist ideas and distort these to suit their own purposes. So, Bell says that the "claim for 'equality of result' is a socialist ethic (as equality of opportunity is the liberal ethic)".[2]

But there is a fundamental distinction between the Marxist and the bourgeois approach to the problems of equality. The chief principle of Marxism, formulated in the *Manifesto of the Communist Party* says: "The free development of each is the condition for the free development of all."[3]

This principle implies the allround development of the individual based on changes in the form of property and the purpose of work. As every individual comes to regard the benefit of society as his vital goal, he acquires an equal right to satisfy his reasonable requirements with a view to the income produced by the whole of society and distri-

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[1] Daniel Bell, *op. cit.*, pp. 411, 425, 443.

[2] *Ibid.*, p. 433.

[3] Karl Marx and Frederick Engels, "Manifesto of the Communist Party". In: Karl Marx and Frederick Engels, *Collected Works*, Vol. 6, p. 506.

buted in accordance with the requirements of the communist-minded individual, who has shed the capitalist private-property mentality. The way to such equality does not lie through a social transformation of capitalism, but through the revolutionary socialist transformation of society, as the class struggle inevitably releases the productive forces from the fetters of the obsolete relations of production.

Bell claims that

> "a new social system, contrary to Marx, does not always arise necessarily within the shell of an old one but sometimes outside of it".[1]

Ignoring such a real historical fact as the bourgeois revolutions that overthrew the power of the feudals, he says that capitalism arose outside the feudal estates, in free communes and towns, which, he says, were socially independent of the feudals. He believes that science centres could play a similar role for the development of the "post-industrial society". He contrasts Big Business with Big Science, whose advantage is that "it has no ideology". Its principle is permanent revolution and renunciation of religious dogmas, to which he refers communism.

So, the "post-Marxist" Bell, who objects to Marx's "much too abstract" analysis in Volume One of *Capital* and urges economists to look to Volume Three, which, he says, is closer to concrete reality, concludes his own analysis of capitalism by totally abstracting himself both from Volume Three of *Capital* and from present-day realities, coming up with a "permanent revolution" which is carried out by Big Science and which is allegedly purged of all ideology. At first glance, Bell departs not only from economic realities, but also from politics. That, however, is not so.

[1] Daniel Bell, *op. cit.*, p. 378.

A closer analysis of his work will show that he substantiates his conclusions not only with the postulates of positivist philosophy, but also with some dogmas of vulgar bourgeois economics. To explain the emergence of a scientific elite within the capitalist framework, he uses the theory of "human capital", and starts from marginalist premises in explaining the need for planning in the "post-industrial society".[1]

It is hardly surprising that Bell's "permanent scientific revolution", as it will be shown later on, provides the methodological basis for long-term forecasting, which. Bell and his followers hope, will help to stabilise capitalism.

4. Techno-Economic and Politico-Economic Aspects of Bourgeois Futurology

The doctrine of "post-industrial society", in spite of its patently utopian social forecasts, provided the philosophical rationale for the use of so-called technological imperatives in concrete complex techno-economic forecasts relating to long-term state-monopoly programming of the economy. Since the mid-1960s, a "prognostication industry" has been rapidly developing in the capitalist countries, where complex teams of experts play the decisive role. Taking the "post-industrial society" doctrine as a point of departure or, more often, as a pretext, these experts frame various long-term programmes under contracts from the government or private corporations on the required scale: global, national, regional, sectoral or corporate.

There is no point in analysing all these forecasts, for much has already been written on this subject by Marxist researchers. We shall confine ourselves to aspects of futurology reflecting the concepts of

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[1] Daniel Bell, *op. cit.*, pp. 440, 467.

present-day bourgeois economics, which makes pragmatic use of its theories of the social transformation of capitalism to realise the goals facing the various nationally specific systems of state-monopoly capitalism.

The substance and purpose of such long-term forecasts, which dovetail with the ideas of "post-industrial society", are best exemplified by the United States, which now leads the capitalist world in this area.

One of the earliest and most popular forecasts for the development of the capitalist economy until the year 2000 was published in the United States with an introduction by Daniel Bell.[1] (Characteristically, the volume was chiefly compiled by staff members of the Hudson Institute which caters for the Pentagon and is headed by the physicist Herman Kahn, the well-known specialist in the strategy of nuclear warfare.)

The working groups that framed the various sections of the forecast took as predicate the assumption that the United States was becoming a post-industrial society, which Bell defined as one

> "in which the organisation of theoretical knowledge becomes paramount for innovation in the society, and in which intellectual institutions become central in the social structure. The statistical baselines and alternative futures are sketched in this volume."[2]

As Bell puts it, it "is not an exercise in prophecy; it is an effort to sketch the constraints of social choice."[3]

How is this done? In accordance with the global goals of US state-monopoly capitalism, the authors

[1] See: Herman Kahn and Anthony J. Wiener, *The Year 2000. A Framework for Speculation on the Next Thirty-Three Years*, The Macmillan Co. Ltd., New York, 1967.

[2] *Ibid.*, p. XXVII.

[3] *Ibid.*, p. XXVIII.

of the book try to sketch the future of the whole world, because, as Bell sees it, the imperatives of the scientific and technical revolution will carry the whole world in the wake of the United States, which is becoming a "post-industrial society" and presents a model of the future for the whole of mankind.

The forecast, as it follows from Bell's methodology, attaches paramount importance to those social institutions which lie outside the industrial nucleus of the economy. Consequently, economic analysis proper does not play the decisive role in the volume, but is swamped in data relating to a superfluous statistical and techno-economic analysis of the sectoral structures of different societies, on the strength of which the researchers pinpoint their place on the road to the "post-industrial society". They also devote much attention to describing various versions of social change and to various sociological conceptions.

Economic forecasts are based on the method of extrapolation, on a "quantitative scenario", where the parameters are population growth, labour productivity growth with a view to the latest technology, and a balanced increase in the gross product on the assumption that there will be no deep depressions in the final third of the century.

We know that historical reality has introduced a significant correction into that "quantitative scenario" at the very beginning of the forecasted period. At the end of 1973, the United States and other developed capitalist countries, poised on the threshold of a "post-industrial society", became the scene of the worst economic crisis since the 1930s, which confirmed that capitalism cannot safeguard the peoples of these countries from crisis upheavals and ensure balanced economic growth with rising living standards. One specific feature of that crisis was that it brought not only mass unemployment, but also inflation, which has become a chronic disease of present-day state-monopoly capitalism.

The cyclical processes that marked the development of the crisis also worsened the energy crisis, engendered by the deep-going changes in the structure of the world capitalist economy as a result of the bankruptcy of neocolonialist policy, which had enabled the developed capitalist countries to buy oil in colonial and semi-colonial countries at monopoly-low prices.

Naturally, the "quantitative scenario" could not have predicted such qualitative changes, whereas for creative Marxist-Leninist thought, which takes due account of the uniformities of the national liberation movement and regards the collapse of the imperialist structure of the world capitalist economy as inevitable, these changes were not unexpected.

The forecast for the social transformations of "post-industrial society" based on an analysis of the techno-economic changes in the production structure and the occupational makeup of the population were equally short-sighted. In their attempts to forecast not only the quantitative, but also the qualitative changes that would occur with the development of the "post-industrial society", the Hudson team predicted that as the share of the population employed in industry declined, the market would play a less important role, as compared with the public sector. As a result, such values as the urge to work, to achieve success and promotion would no longer be as important among the middle strata of society as they used to be, while the sensate and humanist criteria would become central.[1]

Life itself, with the intensifying competition of the 1970s, shows that these forecasts were utopian and out of touch with reality, and that it is absurd to say that the urge to work is a depreciating value, for the struggle for genuine full employment has now become a major goal not only for the workers,

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[1] Herman Kahn and Anthony J. Wiener, *op. cit.*, p. 186.

but also for scientists and technicians who fell victim to mass lay-offs during the crisis.

The bulk of the forecasts for the year 2000 consists of an analysis of sociological concepts, something of an anthology of anti-Marxist doctrines, anti-communist dogmas and sophistic arguments to prove capitalism's social transformations into a "post-industrial society".

But it is not only for performing this ideological function that the Hudson Institute is so generously financed by the US government and the big corporations, for considerable practical importance also attaches to the Hudson team's forecasts on the development of science and technology, compiled on the basis of expert evaluations by leading specialists. In our day, the most daring and seemingly fantastic scientific ideas are at once taken up by the big corporations for further research and development, and are used as guidelines for state technical policy and long-term economic programming in close contact with these corporations.

But even this—the most realistic—part of the forecast, characterising some objective trends in the development of the productive forces, is used in US bourgeois futurology to justify the claims of US state-monopoly capitalism to world domination. In point of fact, that was the main purpose of the Hudson forecast.

It has also been succinctly expressed by the well-known US politologist Zbigniew Brzezinski in his book, *Between Two Ages. America's Role in the Technetronic Era.* As Bell's follower and using his methodology, Brzezinski determined the uniformities of the global political process and the ways to ensure US world domination on the basis of technological imperatives.

Taking all of Bell's postulates on the "post-industrial society" as an axiom, Brzezinski introduces the term "technetronic society" to underline his ideas that the developed capitalist countries "are entering an age in which technology and especially electronics ... are increasingly becoming the principal determinants of social change, altering the mores, the social structure, the values, and the global outlook of society."[1]

Characteristically, Brzezinski abstracts himself from the relations of production to an even greater degree than Bell. He seeks to prove that the changes in the world today are not due to the social revolution, whose banner was first raised by the Soviet Republic in 1917, but to a technetronic revolution led by the United States, where it started after the Second World War. Ignoring the fundamental historical changes in the world brought about by the victories of socialism and by the incentives these created for technological advance itself, Brzezinski maintains that the United States is "the world's social laboratory",[2] the main force capable of saving mankind from revolutionary chaos. He says that unless the United States goes on using its preponderant influence to give "positive" direction to the accelerating pace of change (that is, unless the United States continues to hold back the development of the revolutionary forces),

"that change not only might become chaos ... but could eventually threaten the effort to improve the nature and the character of American domestic life."[3]

While analysing global political processes, Brzezinski utterly ignores such economic categories as the world economy and global economic ties, and also the historically conditioned uniformities of

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[1] Zbigniew Brzezinski, *Between Two Ages. America's Role in the Technetronic Era*, The Viking Press, New York, 1970, p. XIV.
[2] *Ibid.*, p. 196.
[3] *Ibid.*, pp. 307-308.

the class struggle, which determine the irrepressible dynamics of the world revolutionary process. He believes that in the coming technetronic era the course of world events will be determined by the gradual formation of a new global human consciousness, vested in "transnational elites", called upon to govern the backward majority of mankind, who have come to believe, under Marxist influence, that their problems can be solved through revolutionary coercion.

Brzezinski believes that Marxism is outdated, and that the social consciousness of our day is striving for a new intellectual synthesis similar to that effected by Marxism in the industrial epoch.

Since bourgeois economists have not been able to counter Marxism with a synthesis of their own, the task has now been taken over by the politologists. Brzezinski and others spin out stunningly "new" anti-communist doctrines in order to prevent the penetration of Marxist ideas into the minds of the young, inclined to look for new left and radical concepts.

But politology alone cannot fill the ideological vacuum in bourgeois economics, even when it is a matter of prognosticating the future. The society of the future must have a definite economic structure, and so Brzezinski, the anti-communist politologist, turns into a "trail-blazing" economist who takes the theory of the "post-industrial society" a step farther. He singles out three sectors in the US economy:

—technetronic, which includes the new industries, the mass media, and science institutions;

—industrial, which includes the traditional industries with well-paid workers;

—and pre-industrial, which employs low-skilled workers with incomes below average and insufficient access to education, and which also includes racially oppressed groups of the population.

The pre-industrial sector is the chief source of social upheavals. According to Brzezinski, these can be eliminated with the help of measures aimed to increase incomes in the poverty zone, for American society as a whole "is achieving an unprecedented affluence that touches all classes".[1] If social and political stability is to be ensured, he believes, the annual average GNP has to continue growing by 3.5 per cent.

As we find, Brzezinski's innovation in forecasting economic development does not go beyond the commonplace concoctions of the most conservative spokesmen of bourgeois reformism.

In the technetronic era, which, Brzezinski thinks, makes it impossible to attain communist goals in the developed capitalist countries,

> "the active shaping of the future passes into the hands of a socially somewhat conservative but technologically innovative elite".[2]

In contrast to the "new left", who challenge the authoritarian rule of the monopolies and advocate participatory democracy, Brzezinski maintains that such democracy is likely to emerge through a

> "symbiosis of the institutions of society and of government rather than through ... economic expropriation and political revolution, both distinctly anachronistic remedies of the earlier industrial era."[3]

In other words, Brzezinski's idea is that the technetronic revolution can most successfully unfold within the framework of state-monopoly capitalism.

Let us now look at France, the leading European country in the area of long-term economic programming. Jean Fourastié, head of the economics department at the High School of Practical Research, is

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[1] Zbigniew Brzezinski, *op. cit.*, p. 205.
[2] *Ibid.*, p. 248.
[3] *Ibid.*, p. 264.

the best-known theorist who has elaborated future-oriented versions of the "post-industrial society" for France. We have already mentioned his works, where he seeks to prove that the scientific and technical revolution invalidates the doctrine of class struggle and leads to an automatic solution of all social problems by creating a "consumer society", or a so-called "tertiary civilisation", where the whole economy is pivoted on the service industry.

It was largely under Fourastié's influence that a prognostic long-term aspect was introduced into indicative medium-term planning by the state in order to convince the masses that society can be improved with the help of bourgeois reforms in the economy.

Accentuating the criterion of technological progress, Fourastié criticises traditional bourgeois political economy, accusing it of a static approach and of orientation upon equilibrium and constant prices, and arguing that technological progress makes society much more dynamic, with ceaseless perturbations in the structure of production, distribution, consumption, and prices.

That is why any economic programme should contain a prognostic element and should be oriented upon the future. At the same time, Fourastié's forecasts are meant to prove that it is quite possible to ensure social stability in a dynamic society based on technological progress.

In his book, *The Civilisation of 1995*,[1] he elaborates his basic idea in this spirit: a revolutionary redivision of the national wealth cannot improve the nation's life, whereas economic growth deriving from technological progress does this very well by creating a "civilisation of leisure". Such a civilisation reduces the incentive for the individual to increase his income by working more at the expense

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[1] Jean Fourastié, *La civilisation de 1995*, Presses universitaires de France, Paris, 1970.

of his leisure time. Fourastié maintains that as labour is eased out by machinery from the primary and secondary sectors, it will be employed in the tertiary sector. Since there are no incentives in the latter for rapid technological progress and greater unemployment, this sector will be the factor ensuring the social stability of the whole economy.

The 1960s showed, however, that technological progress and economic growth did not ensure social stability, blasting Fourastié's hope that the managers, using the methods of social engineering and social psychology, using the "human relations" tactics at the enterprises and in the institutions, and taking steps to organise the masses' leisure on the "bread and circuses" principle, would be able to put an end to the class struggle aimed against the "harmony of social stability". Moreover, the leisure problem has itself become the target of class struggle. The younger generation is disenchanted with the philistine ideals of the "consumer society" and is carrying on a vigorous struggle for educational reform, for opportunities not only to improve their professional skills to meet the demands of technological progress, but also to satisfy their spiritual requirements.

Fourastié's book, *An Open Letter to Four Billion Men*,[1] reflected his disappointment in technological progress. His reasoning now takes a turn similar to Raymond Aron's. Fourastié explains the absence of social stability in the "tertiary civilisation" by psychological factors, on the assumptions of anthropological philosophy concerning the correlation between the conscious and the subconscious in man's motivations.

The whole point, he believes, is that the technical environment frustrates man's intrinsic urge to be close to nature, and this causes neuroses, which lead to outbursts of discontent. Fourastié concludes

[1] Jean Fourastié, *Lettre ouverte à quatre milliards d'hommes*, Editions Albin Michel, Paris, 1970.

that one should give up the illusion that man can live in a rationalised world. To solve the problem of social stability, the "post-industrial society" should restore the natural balance of man's existence that has been upset by "industrialism" and "urbanism". The best use of leisure time is creative work, which promotes the individual's harmonious development. But it is only the elite that is capable of such work. Fourastié is not sure that the "quaternary" civilisation will be able to bridge the gap between the elite and the masses, to inspire the masses with a thirst for knowledge, for creative scientific endeavour and a meaningful spiritual life. Although Fourastié borrows from Marxism the idea of the individual's allround development, he cannot overcome his bourgeois outlook and recognise the need to eliminate society's division into an elite and the mass.

In France, where socialist ideas have deep roots, the practice of borrowing Marxist ideas in order to fight Marxism itself leaves an imprint on long-term development programmes reflecting the strategic goals of state-monopoly capitalism. Take the forecast for 1985 framed by a team of specialists with Fourastié's participation and submitted to the French Commissariat for Planning as material to be considered in drawing up the plan for 1965-1970.[1] It formulates the politico-economic and social principles showing that the "American way of life" is unacceptable for France. It also points out the way to raise its competitiveness on the world market so as to secure a leading position in the European Economic Community and to meet the "US challenge". Here are some of its provisions.

By 1985, there is to be a transition from the society of necessity to a society of expression, which is a sign of freedom; every citizen is to be involved

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[1] See: *Reflexions pour 1985. La documentation française*, Paris, 1964.

in the life of the nation, work and leisure are to blend into a single form of activity conducive to man's allround development; aesthetics is to be the measure of well-being in the new civilisation, for man can realise himself in society only when he can satisfy his aesthetic aspirations.

So much for that which one might call the poetry of the future.

And here is the prose, reflecting the interests of Big Business: state revenue from taxes should not undermine the spirit of enterprise and innovation, and also the propensity to save. France is to take part in the European mass-production economy, and it is necessary therefore to set up a system of programming on a European scale in the field of transport, oil and gas pipelines, metallurgy, chemistry, oil refining, the nuclear power industry and water supply. The "US challenge" necessitates rapid growth.

Such are some of the elements of the harmonious "quaternary" civilisation as spelled out in the forecast which lays down guidelines for state-monopoly programming.

The theories of capitalism's social transformation and the closely related concept of the convergence of the two systems arose, have developed and are being constantly renewed in view of the attempts on the part of bourgeois economists to produce an antithesis to Marxism. As the influence of the Marxist-Leninist theory has strengthened and extended, they have been working ever harder in this direction. Still, they have failed to produce an integral theory to counter Marxism-Leninism, in spite of the symbiosis of economic and sociological concepts in theories of capitalism's social transformation.

Why is that so? First of all, the Marxist-Leninist theory is essentially revolutionary and its approach is intrinsically historical, for it maintains that the prerequisites of the future are to be found in the past and present. In its analysis, it takes due account of the close interrelationship between the productive forces and the relations of production (society's basis), and also between the basis and the superstructure: the state, and philosophical, juridical and other notions. It sets itself the task not only to explain the world, but also to change it by developing the class struggle, which culminates in the victory of the working class and the formation of a classless society. Under socialism—the first phase of communism—the class struggle comes to an end and the way is opened for society's evolution to communism, which will ensure the allround development of the individual, society's chief productive force.

What is the antithesis to Marxism-Leninism as formulated by the advocates of capitalism's social transformation? They fail to see the connection between the logic of ideas and the logic of things, detaching the productive forces from the relations of production, depriving society of a mechanism of self-propulsion, and regarding it as an elite-controlled structure which has to be "harmonised" without the participation of the masses, whose revolutionary consciousness has to be extinguished by bourgeois apologetics in order to confine the class struggle to the framework of a stable social structure. According to the latest ideas of bourgeois futurologists, even revolutionary changes in technology should be checked as soon as they create social tensions that could jeopardise the capitalist system. In the final count, the theories advocating society's subordination to technological imperatives are deeply conservative and are directed against any fundamental socio-economic transformation of the capitalist society.

CHAPTER TEN

THE ECONOMIC THEORY OF MANAGERIAL CAPITALISM

The large corporation has become a major target of research across the whole spectrum of social sciences in the West. It is being considered from different angles: politico-economic, juridical, and socio-class. The reasons for such a lively interest are obvious: the large corporations concentrate an ever greater share of production and resources at the crucial stages and in the key sectors of the economy.

The theorists of managerialism devote much attention to the large corporation. They have inherited such theoretical propositions of bourgeois political economy as the thesis about the separation of ownership from control in the large corporation or the doctrine of the "managerial revolution", which have been thoroughly criticised in Marxist writings.[1]

The new elements in managerialism are due to the complexification of the social and organisational structure of the capitalist corporation, which in-

[1] See, for instance, S. M. Menshikov, *Millionaires and Managers*, Mysl Publishers, Moscow, 1965; I. I. Beglov, *USA: Property and Power*, Nauka Publishing House, Moscow, 1971; *A Political Economy of Present-Day Monopoly Capitalism*, Vol. I, Chapter IX, Mysl Publishers, Moscow, 1975 (all in Russian).

duces Western theorists somewhat to modify their approach to the set of problems relating to the functioning of the joint-stock form of property.

Today, the central problems in this area relate to the principles governing the activity of the large corporation in contrast to the laws of the market, notably the securities market (fictitious capital). This contrast, as I shall try to show, reflects some essential contradictions of present-day capitalism.

1. "Dispersion" of Joint-Stock Property and the Problem of Control

The notion of separation of ownership from control in the large corporation[1] has been taken as a point of departure by the managerialists, who have borrowed it from the institutionalists. Its role in the evolution of the bourgeois theory of the firm is so important that its latest aspects need to be considered in greater detail.

According to the notion of separation, control (power) in the large corporations of the developed capitalist countries is going over (or has already gone over) from the capitalist owners to career managers. Here is how a leading managerialist formulates this notion, which relates to the functioning of the whole capitalist system:

> "'Managerial' capitalism is a name for the economic system of North America and Western Europe in the mid-twentieth century, a system in which production is concentrated in the hands of large joint-stock companies. In many sectors of economic activity the classical entrepreneur has virtually disappeared. ...As a result ... entrepreneurship in the modern corporation has been taken over by transcendent management, whose functions

[1] Subsequently, just "the notion of separation".

differ in kind from those of the traditional subordinate or 'mere manager'. These people...can wield considerable power without necessarily holding equity, sharing profits or carrying risks."[1]

The terms "managerial power" and "managerial control" are widely used in managerialist theories but such categorical statements do not show whose interests are voiced by the "transcendent management" of the large corporations, and say nothing about their economic and social nature. That is why one has to analyse the definitions of the basic categories—ownership and control—in the works of managerialists.

The object they are considering—the large corporation—determines the limits in which the category of ownership is defined. They confine it to ownership of joint-stock capital or, to be more precise, of "common" (or voting) shares. The accent here is on the "dispersion" (or diffusion) of share capital, which is seen as the reason behind the weakening or rupture of ties between ownership and control.

Naturally, it is most important to study the diffusion of share capital. But what does such diffusion actually mean? It can mean an exceptionally high concentration of control in the hands of a few big shareholders. Moreover, the partial erosion of the ownership—control nexus, even if this does take place, does not predetermine the ultimate outcome, that is, where the control in the large corporation is transferred.[2]

Indeed, as the ownership—control nexus weakens, power in the large corporations is deprived

[1] Robin Marris, *The Economic Theory of "Managerial" Capitalism*, Macmillan and Co. Ltd., London, 1964, p. 4.

[2] This peculiar feature of the separation notion was noted by the Belgian researcher Michel de Vroey: "On the one hand, it refers to the dispersion of shares among a large public in large corporations. Its consequence is the emergence of a new type of owner—the absentee stockholder.

of its base and, in effect, hangs poised in mid-air. Western theorists prop up this baseless power with the career manager. However, they do not define this manager in social terms, so that his image is a social abstraction in the full sense of the word. As a result, the problem is further obscured.

Western researchers have mustered a large array of data to substantiate the separation notion, and have calculated the degree of separation. But none of their calculations show how the power base has shifted. Let us compare the figures given by the US economist R. Larner and the French economist J. M. Chevalier on the concentration of share capital in 104 of the 200 largest US corporations. Larner maintains that corporations can be subjected to meaningful stockholder control if an individual or a family owns 10 per cent of the stock, while Chevalier contends that the figure is only 5 per cent.[1]

But such conclusions have one defect deriving from the methodology of analysis: capitalist property is equated with juridical private ownership of "voting" shares in the corporation. Accordingly, sight is lost of the complex interaction between individual and family ownership of shares with the institutional system of capitalism (including the system of financial institutions), whose analysis is the only way to bring out the modern forms of private capitalist property in all their variety. As soon as some researcher comes to the conclusion that in a given corporation there is not a single

... On the other hand, the notion points to a shift of the power base within the corporation. ...A conclusion derived from verifying the first sense cannot be simply extended to the second." (Michel de Vroey, "The Owners' Interventions in Decision-Making in Large Corporations". In: *European Economic Review*, Vol. 6, No. 1, January 1975, pp. 1-2.)

[1] J. M. Chevalier, "The Problem of Control in Large American Corporations", *Antitrust Bulletin*, Spring 1969. Quoted from: John M. Blair, *Economic Concentration. Structure, Behavior and Public Policy*, Harcourt Brace Jovanovich, Inc., New York, 1972. p. 80.

shareholder who can influence the decision-making process, either by himself or in coalition with other shareholders, the corporation is promptly switched from the private-capitalist to the "managerial" department.[1]

Research into joint-stock ownership in the large corporations gave rise to disputes over the distinctions between the structural and functional unity of ownership and control. A point to note is that the difference of opinion on this issue reflected the deep schism in bourgeois economics on the problem of ownership under present-day capitalism. Economists of the traditional schools insisted on the unity of ownership and management, saying that the large corporation has not introduced any essentially new elements into the relations of capitalist ownership. Their opponents emphasised the special role of managers and said that the large corporation stood in basic opposition to "capital" and to private property in general. What did they mean? By structure of ownership and control they meant the formal juridical signs of dispersion (concentration) of share capital, the presence (or absence) of big stockholders or allied groups of stockholders on the board of directors and, in consequence of this, the relative independence of managers in decision-making. Many researchers agreed that in this (largely nominal) respect the unity of ownership and control was disrupted. But at the same time, they believed that as regards the *functioning* of the corporations (i.e.

[1] The latest edition of S. Florence's book, *The Logic of British and American Industry* (London, 1972), contains extensive data to show how relative the dividing line is in evaluating the power base in a big corporation.

Florence points to E. Penrose's calculations, which show how effective control can be exercised by the owner of 3-5 per cent of the stock, provided the degree of dispersion is considerable. (See: S. Florence, *op. cit.*, p. 375.) But control through relatively small shareholdings is possible only so long as the management is stable. When the struggle for a change of management or for a merger gets under way, even a 30 per cent block of "voting" shares is often insufficient.

as regards the identity of interests of the owners and managers) such unity was fully preserved.

The economic part of the argument in favour of such functional unity of ownership and control includes an analysis of the forms of remuneration of top executives. There are two views on this point: first, that their incomes primarily depend on the growth of the firm (its sales, shipments, fixed assets); and second, that these incomes largely depend on the growth of profit.

Is there any contradiction between these two indicators—growth of the firm and growth of profits?

There is no doubt at all that this is a possible and real contradiction in the foreseeable period which is usually covered by current planning of the firm's activity. A limit on the growth of profits and, above all, of dividends, and a step-up of the firm's growth through various sources of financing could prove to be highly disadvantageous for stockholders. Neoclassical theory assumes that in this case the temporary loss of dividends is compensated by the growth of the market price of stocks, which is a reflection of the overall economic strength of the corporation and its capacity to pay higher dividends in the future. But in practice, this assumption of neoclassical theory about a "perfect trade-off" between earnings on capital in the present (through dividends) and in the future (through stock prices) is not justified. The stockholder may never be compensated for such a loss of dividends. Consequently, it is not at all a matter of indifference to the stockholder (including the big stockholder who is capable of exerting an influence on corporation policy) which way of development the corporation opts for.

The incomes of top executives are made up from various sources: salary, bonuses on the strength of sales and profit, and so-called stock options. Option is the executive's right to buy sizeable holdings of his corporation's stock at face value. The executive makes use of this right in the event of a rise in stock-market prices. Thus, bonuses for profits and stock options are a means of stimulating the capitalist results of the corporation's activity tying in the executive's interests in practice with those of the capitalist owners. Besides, this form of incentive inevitably turns the executive into a stockholding co-owner of the corporation.

The analysis of the sources from which the incomes of top executives are formed has produced highly contradictory results. Robert Gordon, a well-known analyst of the role of executives in the large corporation, has reached the conclusion that the growth of company size is the basic variable on which the growth of executive incomes depends. Salary and bonus for the growth of sales were the dominant financial incentive held out to the top executives, according to a study carried out by Gordon in the 1930s.[1] Samuel Reid quotes the *American Economic Review*:

> "The evidence presented would seem to support the likelihood that there is a valid relationship between sales and executive incomes ... but not between profits and executive incomes."[2]

He believes that these data are an empirical confirmation of Baumol's assumption that maximisation of sales is the target function of the large company (we shall consider below the question of the company's target function in management theories).

We find the very opposite view in other empirical statistical studies. Thus, Wilbur Lewellen rejects Gordon's view and says that from 1955 to 1963

> "salary and bonus accounted for only 38 per cent of the total after-tax remuneration of

[1] Robert Aaron Gordon, *Business Leadership in the Large Corporation*, University of California Press, Berkeley and Los Angeles, 1961, p. 301.

[2] Samuel Richardson Reid, *Mergers, Managers and the Economy*, McGraw-Hill Book Company, New York, 1968, p. 135.

the top executive in each of the 50 companies, while deferred and contingent forms of compensation accounted for 47 per cent of the total, with stock options alone accounting for 36 per cent".[1]

This is supported by Robert Larner, who believes that direct deductions from profits in various forms constitute a growing share of executive incomes. That, he believes, effectively ties in the interests of executives with those of the stockholders. Let us note that this view was expressed in a book designed to prove the continued structural separation of ownership from control. In spite of this, the author believes that these owners have been regaining their influence on the level of large corporation policy and its actual results. This view indicates a most important channel through which stockholdings influence management, namely, the form of executive remuneration.[2]

It is not surprising that such different and even contradictory data from concrete studies lead their authors to make the very opposite conclusions concerning the nature of the interaction of ownership—control—management factors in the large corporation. Reid says that there is not just separation of ownership from control, as Berle and Means said many years ago, but a conflict of interest.[3]

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[1] Wilbur Lewellen, *Executive Compensation in Large Industrial Corporations*, National Bureau of Economic Research, New York, 1968, p. 141.

[2] "The average expected dividends and capital gains from stockholdings earned by the chief executive officers in our sample amounted to $ 64,519 per year. Although managers may hold only a small fraction of the outstanding common stock in the typical large corporation, still the dollar value of their stockholdings is large enough to give them an important stockholder interest in the enterprise they manage." (Robert J. Larner, *Management, Control and the Large Corporation*, Dunellen Publishing Company, Inc., Cambr. (Mass.), 1970, p. 66).

[3] See: Samuel Richardson Reid, *op. cit.*, p. 153.

By contrast, Larner believes that

> "managers ... are a tiny (in numbers) subset within the larger set of all stockholders, and not a completely separate group with distinct interests that conflict with those of stockholders".

He adds that

> "the pecuniary interest of managers" is effectively linked to the "pecuniary interest of stockholders".[1]

This discrepancy makes one assume that the problem to whose solution these results relate was formulated incorrectly from the very outset. I have already said that in social terms the contraposition of career managers and stockholder-owners is much too abstract.

The schism between the purposes of capital and the purposes of the scientific management of production is a real contradiction of modern capitalism. But in managerial theory it is presented as an antagonism between the mass of managers (taken as a whole) and the stockholder-owners, i.e., it is presented in a form without any social content. Such is the method of the Western "positive" sciences in social research: while denying the class nature of social phenomena, they seek to draw the most general and apparently non-social conclusions concerning the consequences of technological and organisational progress.

2. Stock Capital and Private Property. Concerning the "Waning" of the Capitalist— the Private Entrepreneur

The earlier separation argument based on the calculation of the extent to which stock capital is "dispersed" may be said to have finally compromised itself. In these conditions, the radical left wing of bourgeois economics seeks to consider the problem

[1] Robert J. Larner, *op. cit.*, pp. 63, 66.

of control in the large corporation from a different angle. Thus, de Vroey regards the exercise of control in the large corporation as being the result of the interaction of property structures and management structures. He asserts that an analysis of the interaction of these structures helps to establish the intensity of the influence exerted by the property factor on decision-making at various levels. Having analysed 40 large capitalist corporations in Belgium from this angle, the author reached the conclusion that in 26 cases, at the very least, the property factor exerts a crucial influence on decision-making (in nine other cases, Belgian companies turned out to be subsidiaries of foreign corporations, so that the nature of control remained undecided). De Vroey made the reservation that Belgian companies are much smaller than the largest US or even European companies.

Nevertheless, this does not refute something like a rational approach by the author which tends to overcome the mechanical contrast between "managerial" companies and "family" companies.

Besides, such studies are a fresh warning against any mechanical application of the trends going forward in the United States to all the other developed capitalist countries. The separation has been developed on US soil and on US data. But the fact is that with respect to the diffusion of stock capital and the role of "family", "dynastic" fortunes in corporation control, the picture in some "small" capitalist countries is totally different from the one we find in the United States.

When criticising the idea of the diffusion of fictitious capital, one must return again to the widely accepted theory which claims that the role of private property in modern capitalism tends to wane, that private property is being pushed well into the background, giving place to "institutions" like banks, insurance companies, industrial corporations, etc. Actually, stockholdings continue to be one of the most important and crucial forms of capitalist property. In this light one must consider the myth about the disappearance of the capitalist in the world of large corporations, and his transformation into a passive stockholder deprived of power, or, as Berle put it,

> "the capital is there; and so is capitalism. The waning factor is the capitalist."[1]

Stockholdings are the fastest and most effective way of increasing personal fortunes. This will be seen from a comparison of the price index for "common" stock with the price index of other securities over a long period.[2] Despite the steady and marked growth in the number of small stockholders, stockholding is an effective way of establishing control for those who seek to do so. But even in the hands of the small stockholder this is not at all an innocent title to a small additional income. The small stockholders also "vote", and the latest wave of monopoly mergers which rolled across the developed capitalist countries in the late 1960s and early 1970s showed that some groups of capitalists allied themselves with the small stockholders against other groups of big capital in the course of "takeovers" and associations. The theory of the stockholder's "euthanasia" was swamped in the great tide of mergers managed mainly along the stockholding—control connection.[3]

The capitalists are well aware of the special role of stocks among all the other types of securities and

[1] Adolf A. Berle, Jr. *The Twentieth Century Capitalist Revolution*, Harcourt, Brace and Co., New York, 1954, p. 39.

[2] From 1960 to 1972, the Dow-Jones industrial average increased by more than 50 per cent. In that same period, the prices of securities—government, municipal and corporate—registered a marked drop. The only year stock prices fell markedly was 1970. (See: *Statistical Abstract of the US*, 1973, p. 459.)

[3] It was A. Berle who put forward the theory of the stockholder's "euthanasia" as evidence of the bureaucrat's takeover from the capitalist. (See: Adolf A. Berle, *op. cit.*)

property titles. The share of stock capital among all the other forms of corporation finance has been relatively small over the whole postwar period. The corporations are highly cautious and use additional stock issues as a last resort, preferring other forms of finance which are less connected with a division of power.[1] Finally, despite the gradual growth of the proportion of financial institutions in the ownership of stock capital in the leading capitalist countries, more than one-half (and in the United States nearly three-quarters) of stock capital is individually owned.[2] The bulk of individual stock capital is concentrated in a few hands. Stock capital remains the favoured form for the investment of the largest personal fortunes, and this refutes Berle's theory about the "institutionalisation" of ownership, and with it, of control.[3]

[1] The share of new common stock issues within the overall structure of external corporate finance will be seen from a comparison of the following data on the issue of common stock and the data on the issue of other corporate "liabilities" (bonds, preferred stock, mortgage, etc.).

Annual sales of US corporate securities (mill. dollars):

	1960	1965	1970	1972
All types of securities	10,154	15,992	38,945	41,975
including:				
common stock	1,664	1,547	7,240	9,694
per cent	16.4	9.6	18.6	23.2

(*Statistical Abstract of the US*, 1973, p. 461.)

While stock remains a secondary source of external corporate finance, its share has been growing since 1965, a fact connected with the growth of mergers entailing a substitution of the new "juridical person's" stock for the merged companies' stock.

[2] In the United States, a comparison of the condition of individual stockholders (as a group) with that of financial institutions (as a group) shows that in 1968 the former accounted for 73.2 per cent of all the stock issued by industrial and financial corporations according to market prices. The holders of 75 per cent of the individually owned stock came to only 5 per cent of the total individual stockholders (*Journal of Business*, July 1974).

[3] See: A. Berle, *American Economic Republic*, New York, 1962.

The share of stock capital in the structure of financial sources has been steadily declining. Meanwhile, the charter of the corporation (joint-stock company) in most capitalist countries recognises the stockholders' right of unlimited owners, whereas stock capital now has a dwindling share in corporate property (liabilities). In the 1930s, the share of "common" stock in the structure of balance-sheet liabilities of the US corporate sector came to about 30 per cent, but in 1970, it came to less than 10 per cent.[1] Let us recall that with the wide dispersion of the bulk of stock capital, the ownership of even 5 per cent of the stock gives effective control of the corporation. But 5 per cent of 10 per cent comes to 0.5 per cent, and that is precisely the interest in corporate capital which, according to the most formal calculation, suffices to give the big stockholder or a well-knit group of stockholders control of the corporation.

As I have repeatedly said, no more than 0.1-0.01 per cent of the total number of individual stockholders can actually claim to exercise control in the large corporations.

But there is yet another important aspect to the mechanism by means of which private property rules the economy in the most "generalised" form (in the form of individual stockholdings). The market value of stock capital registered on US stock exchanges is roughly equal to the country's gross national product.[2] These great chunks of fictitious

[1] See: *Statistical Abstract of the US*, 1960, p. 488; 1973, p. 479.

[2] In 1972, stocks worth $ 872 billion were registered on the New York Stock Exchange, whose share of annual turnover is roughly three-quarters of total stock capital turnover. (See: *Statistical Abstract of the US*, 1973, p. 460.) In other words, the total stock capital registered on US stock exchanges could be assessed at $ 1,250 billion (1972), an understatement, because some of the stock did not appear on the stock exchange and is not registered there. In 1972, the GNP of the United States came to about $ 1,100 billion.

capital constitute an assessment of the claims to corporation earnings now and in the future, and at that to the most mobile part of the profit which remains after the deduction of all the hard liabilities. It is well known that capitalist economic growth usually results in an automatic conversion of a growing share of the national income into fictitious capital. Qualitatively, this is expressed in the growing gap between the nominal and the market value of stock capital, whose ratio indicator in the United States went up from 260 per cent in 1960 to 400 per cent in 1970.[1]

These data are among the many testimonials to the tremendous concentration of power in the corporate sector, but they must not obscure the fact that in many of the largest corporations in the capitalist world (like General Motors and ITT) the biggest portfolios do not exceed 0.1 per cent of the stock capital.

How do the channels of control function in such cases? Without going into the whole problem of the movement of finance capital and the contemporary forms of financial groups (these questions go beyond the task set here, namely, a critique of the bourgeois separation thesis), I should like to draw attention to two phenomena in the development of connections between financial institutions and the corporate sector.

The first of these relates to the concentration of large blocks of stock in the trust departments of the major commercial banks. The voting rights which are frequently conveyed to the trust department together with the stock provide the major banks with a powerful instrument for exerting an influence on the policy of the large corporations. Although concrete studies do not show the actual

[1] Estimated from a consolidated balance-sheet of the corporations and an assessment of the total stock capital registered on the stock exchanges (see: *Statistical Abstract of the US*, 1974, pp. 460, 473).

size of the portfolios of individual corporations held by the trust funds of individual banks (the trust funds are, of necessity, widely diversified), there is still no doubt that the banks' overall policy is connected with the interests of fictitious capital, and the trust funds provide an additional instrument of this policy.[1]

The growth of bond issues as a source of external corporate finance is another phenomenon of primary importance in the development of ties between the financial sphere and the processes of actual reproduction. Insurance companies are the chief holders of bonds in the private capitalist sector. The interests of bond holders are far from being identical with those of stockholders. Because bonds are fixed-interest securities their quotations are not subject to such sharp fluctuations as stock quotations and the basis for the floating of a bond issue generally consists in the healthy functioning of real capital over a long period.

The positions of financial institutions are fortified by interlocking directorates, whose extensive spread is confirmed by a number of recent studies.[2]

Returning to Berle's claim about the "waning" of the capitalist, we have good reason to say that even in the sphere to which this assertion applies (namely, the largest capitalist corporations), the

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[1] The size of individual stock capital invested in the trust funds of the major US banks with full or partial transfer of voting rights came to nearly $ 162 billion in 1968. (See: *Commercial Banks and Their Trust Activities*, US Congress Committee on Banking and Currency, Washington, 1968.) According to my estimates, this is about 18-20 per cent of the issued stock capital (market value). The purposeful use of these blocks of "voting" stock can undoubtedly exert a substantial influence on the policy of the major corporations.

[2] Interlocks between industrial and financial institutions are commonplace; of the 1,049 interlocks held by directors of industrials, 36 per cent (378) were found to be with banks and insurance companies. (See: John M. Blair, *Economic Concentration*, New York, 1972, p. 78.)

concentration of stock capital in the form of individual and family fortunes, the interaction and alliance of the owners of these fortunes with the system of capitalist financial institutions, the personal union and the interlocking directorate, all of these ultimately ensure the domination of private-capitalist property.

3. The Growth of the Large Corporation and Its Modelling in Managerial Theories

The discussion between bourgeois economists about the separation of ownership from control gradually petered out without producing any tangible results. There were numerous pros and cons to prove or disprove the "independence" of managers. Meanwhile, the actual processes from which the discussion sprang continued to develop and demanded of the various schools of bourgeois economics a theoretical interpretation. The growth of the absolute size of large corporations, and their ever more complex organisational and financial structure intensified the trend towards the autonomy of the large corporation with respect to the economic environment.[1]

This trend was based on deep-going processes in the concentration of production. The production basis of the large capitalist corporation became ever more complex, and the tasks of setting up and bolstering organisational systems came to the fore. These could not be tackled by means of the old methods of concentration and centralisation of capital. Capitalist associations in the form of trusts and largely also of concerns were based on intricate indirect ties and a shared-stock system, being topped either with a "private" holding or a "parent"

[1] Here autonomy is taken to mean greater potentialities for deliberately influencing the environment.

company. Redistribution and concentration ran through the medium of an intricate system of stockholding. The complexification and growth of organised systems within and outside the old-type capitalist groups called for a substantial change in the methods of financing and allocation of investments. First of all, there was the need for a solid fund to meet the requirements of the new organisational unit. This generated the trend towards the growing autonomy of the large corporation, which consisted in the urge to intensify control over the money flows produced by its own operations.

The exponents of managerial theory put their own interpretation on the mounting trend towards the growing autonomy of the large corporation. Their interpretation is based on a contrast between *organisation* (as some sort of non-social phenomenon) and *finance*, which expresses the capitalist environment.[1] This approach could be interpreted as a modern version of the theories of the US economist and sociologist T. Veblen, who contrasted "industry" and "business", taking the latter to mean everything that is connected with the capital market, the stockholding system, institutionalism, etc. But while it is possible analytically to separate elements of the productive forces from elements of the relations of production, in reality the large corporation is not at all a pure embodiment of "industry" extracted from the social environment, just as finance is not a pure embodiment of capital.

This contraposition brings out one, albeit important, aspect of the process, namely, the growing socialisation of production. But another key aspect of the process is that both "organisation" and "finance" operate as different forms of the movement of

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[1] The economico-institutional essence of managerial capitalism lies in the widespread separation not so much of ownership from control as of organisation from finance. (Robin Marris, *The Economic Theory of "Managerial" Capitalism*, Macmillan and Co. Ltd., London, 1964, p. 33.

capital, each of which fulfils both an exploitive and a real function.

Defining one of the key features of imperialism, Lenin wrote:

> "It is characteristic of capitalism in general that the ownership of capital is separated from the application of capital to production, that money capital is separated from industrial or productive capital, and that the rentier who lives entirely on income obtained from money capital, is separated from the entrepreneur and from all who are directly concerned in the management of capital."[1]

The growing size and importance of the corporation in the economy of all the developed capitalist countries has also led to a simultaneous growth of the whole sphere of fictitious capital. It is this fact of the increasing contraposition of the two key forms of capital that drew the attention of Western analysts, who interpreted them according to their own lights. An examination of this problem makes it possible to go on to an evaluation of managerial theory models and to assess their basic premises and conclusions.

One group of these models is contrasted in present-day bourgeois economics to the neoclassical models of the firm. Let us recall that the basic principle for structuring the neoclassical model is maximisation of net earnings, or profit (P) as the difference between total receipts (TR) and total costs (TC). Maximisation of the function of the

$$P = TR - TC$$

type leads to the basic theorem of the neoclassical model, namely: the firm is in equilibrium when

[1] V. I. Lenin, *Collected Works*, Vol. 22, Progress Publishers, Moscow, 1977, p. 238.

marginal receipts equal marginal costs.[1] This conclusion remains valid for the firm in the conditions of perfect competition, total (sectoral) monopoly, and monopoly competition (differentiation of products, oligopoly).[2] In present-day conditions, the neoclassical model assumes a somewhat different form as applied to the large corporation. Because its stockholders are the nominal owners of the corporation, the neoclassical model regards the market price of the company's stock capital as the function that needs to be maximised, or (in other models) the "value rate", i.e. the relation between the market price of stock capital and net assets.

In contrast to neoclassical theory, managerial theory starts from the assumption that stock capital is only a constraint on the managers' freedom of action. Within the limits of the constraint imposed by the stock and loan capital market, career managers work to maximise their "utility" function.

A number of large-corporation models have been elaborated on the strength of this premise, the best known being those of William Baumol (maximisation of gross sales), Robin Marris (maximisation of the output growth rate), and Oliver Williamson (maximisation of "discretion" expenditures).[3]

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[1] Maximisation of profits requires

$$\frac{dP}{dx} = \frac{d\,(TR)}{dx} - d$$

whence $(TR)' = (TC)'$

(P is rate of profit; x volume of production; TR total receipts; TC total costs).

[2] The neoclassical theory of the firm has been set forth and critically assessed in Antonio Pesenti, *Manuale di economica politica*, Editori Riuniti, Roma, 1970. The neoclassical model in the conditions of "imperfect" competition and monopoly is considered in detail by Joan Robinson in her *Economics of Imperfect Competition*, London, 1962.

[3] See: William J. Baumol, *Business Behaviour, Value and Growth*, The Macmillan Company, New York, 1959; Robin Marris, *op. cit.*; Oliver R. Williamson, *Corporate Control and Business Behaviour*, Prentice Hall, Inc., Englewood Cliffs, New Jersey, 1970.

Baumol's model reflected his experience as a professional consultant of large firms. He got the impression that in most cases the large firms looked to some "adequate" volume of profits and sought to maximise sales.[1] He regards his model as the theoretical backup for the method of "target" profits on capital and "target return pricing policy", adopted by many major US corporations, according to empirical observations.[2]

In a sense, this has provided the starting point for all the subsequent models connected with the managerial theory of the large firm. Baumol believes that only under "pure" competition does the maximisation of profits remain an imperative for the firm's survival. Under monopoly competition, and especially with a high level of intrasectoral concentration and an oligopoly structure of the market, the large firms can choose their strategy for long-term behaviour (target function) which does not necessarily boil down to maximising profit.[3]

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[1] See: William J. Baumol, *op. cit.*

[2] See: A. Kaplan, J. B. Dirlam, R. F. Lanzillotti, *Pricing in Big Business. A Case Approach*, The Brookings Institution, Washington, 1958.

[3] Baumol takes an oligopoly structure as the starting point for his model and does not subsequently examine this question. The important thing for him, as for other managerial theorists, is the internal dynamics of the large firm, and not the problem of interaction between large firms, which is central for the theory of oligopoly and "industrial organisation". This "division of labour" results in the absence of any single theory of monopoly and competition in present-day bourgeois economics. Baumol says: "The discussion so far has been confined to the case of pure competition and has assumed that the firm's objective is to maximize profit. But larger *oligopolistic* firms may well have a different set of objectives. Specifically, I have suggested that management's goal may well be to maximize 'sales' (total revenue) subject to a profit constraint." (William J. Baumol, "On the Theory of Expansion of the Firm". In: *The American Economic Review*, December 1962, No. 5, p. 1085.)

Baumol's model is described by means of the following system of equations[1]:

$$g = f\,(I,\ P),$$
$$I = \Phi\,(P,\ D) + E,$$
$$P = D + E,$$

where g is rate of growth of total revenue; I investments in relation to the firm's capital assets; P rate of profit as interest on stock capital (market value); D dividend as interest on stock capital; and E retained profit as interest on stock capital.

Investments are the strategic variable in the growth rate maximisation model. The rate of profit on stock capital is simultaneously a source of investment and the most important constraint.[2]

Over the long term, the clash between profits and sales leads, in the author's opinion, to a choice of some optimal strategy in which profits are a "manageable" variable, a means for achieving management's goals. The corollary is that there is a substantial discrepancy between the rate of profit and growth rate in the neoclassical model and in Baumol's model, where profits over the long term are lower than the sales growth rate.[3]

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[1] This is a correct model of the maximisation of "sales" growth rate, but its conclusions do not materially differ from the initial model. (*Ibid.*)

[2] Explaining this twofold role of the rate of profit in the model, the author says: "Capital is raised both by direct retention of profits and by the payment of dividends to induce outside investors to provide funds to the company. But, beyond some point, profits compete with sales. For the lower prices and higher marketing outlays which are necessary to promote sales also cut into net earnings." (William J. Baumol, *op. cit.*, pp. 1085-1086.)

[3] For the mathematical proof of this discrepancy, see: William J. Baumol, *Value, Capital and Growth*, pp. 54-56.

This conclusion is directed against the neoclassical theorists who believe that over the long term high growth rates feed profits, and vice versa. For details see: F. Scherer, *Industrial Structure and Economic Performance*, New York, 1972, p. 371.

Baumol's model evokes the following remarks. Its main assumptions contain the old and basic idea of the managerial theorists that "organisation" is moving away from "finance". The "environment" which lays claim to profits and which supplies the firm with funds in the form of loan capital and stock capital is presented as a passive force adjusting itself to management's policy.

This approach results in a substantial defect in the structuring of the model itself: it does not provide for an active response by the "environment" to the policy of optimising profit which seeks to reduce the latter (notably, to reduce dividend payments).

This defect of Baumol's model leads it into an obvious discrepancy with the actual dynamics, where fictitious capital actively intrudes by the most diverse means into the process of decision-making and the strategy of the large corporation.

Large-corporation models were substantially elaborated by Marris. The characteristic feature of his model is the contrast between the managers' considerations of "utility" consisting of maximisation of the rate of output, and their considerations of "security" connected with the stock market and stock capital.

Marris's basic function has the following form:

$$U = U(C', v),$$

where C' (rate of output growth) is the basic independent variable, and v (value rate of stock capital), the basic independent constraint. An increase in the rate of a firm's growth at the expense of the accumulated share of profits could lead to a drop in the quotations of the corporation's stock (via the dividend rate). This fact tends to discipline management in its urge for unlimited expansion. Maximisation of the output growth rate in the light of the key constraints considered above appears to the management as a synthetic expression of diverse "benefits": power, prestige, size of salary.[1]

The following assessment of its main parameters as compared with the neoclassical model fully applies to the Marris model:

> "In economic terms the difference between 'managerial' and 'neo-classical' behaviour may be considerable. ...Managerial utility maximisation must always involve a faster growth rate and, in general, a lower profit rate than would shareholder utility maximisation."[2]

The model reveals the author's belief that the large "managerial" corporation is sufficiently protected from the "capitalist" environment. The author regards the autonomy of the large corporation as an absolute, apparently being unwilling to see that any corporation which acts too independently with respect to its capitalist environment will worsen its positions on the capital market and face the grave danger of being taken over.[3]

Marris's absolutisation of the large corporation's "independence" has determined the structure of his model and its result. The actual confrontation of the various forms of the movement of capital is much more conflicting and "explosive".

The exaggeration of the "manageability" factor in Marris's model has been criticised both in theoretical writings and by the practitioners of capitalist business. Most criticism was levelled at his effort to present all the problems of the large corporation as those of its *internal* management, which

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1 The general mathematical specification of the Marris model includes seven equations, two inequalities and 12 variables (see: Robin Marris, *op. cit.*, p. 235).

2 *Ibid.*, p. 261.

3 The following statement by Marris provides unambiguous evidence of this: "In the modern world, take-over raiders, wherever they occur, are scarce." (*Ibid.*, p. 33.) Subsequent developments have in fact refuted that idea (for details see the next section of this chapter).

is allegedly capable of pursuing the course it has chosen, whatever the combination of factors in the so-called environment, meaning the loan and fictitious capital market. His critics pointed to the allround penetration and interaction of this so-called environment and the internal management, effected in the most diverse ways.[1] Among the ways of restoring the unity of the corporation and its environment indicated by the critics of managerial theory were: "proxy battles" to change the corporate leadership; mergers and takeovers of companies inadequately realising their "market power"; official complaints by groups of "external" stockholders filed with the Securities and Exchange Commission, etc.

In these conditions, managerial theorists were forced to seek ways of improving their positions. They had simultaneously to respond to criticism from the right, from the neoclassics, who accused them of exaggerating the inefficiency and waste within the large corporation protected from the market; and to criticism from the left, from the radical wing, which accused them of failing to expose the monopoly nature of the large corporation and, moreover, of engaging in a downright apologia of capitalism (their conclusions about low prices and high growth rates as compared with the neoclassical model).

Under the impact of this criticism, an attempt to improve the managerial theory was made by Williamson. His approach is characterised by two main innovations: the introduction of the category of "managerial discretion" and the assumption that the large corporation's "utility function" is not always the same, that it could be modified depending on the interaction of external and internal fac-

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[1] See: S. Peterson, "Corporate Control and Capitalism". In: *The Quarterly Journal of Economics*, February 1965, No. 1, pp. 1-25.

tors.[1] Williamson's generalised model of the corporation was designed to reflect the mechanism of this transformation. He remarks that the utilities which are highly valued in the corporate hierarchy include elements which are either not directly expressed in cash terms at all or are reflected in the growth of costs, and limit profits. Among these elements he emphasises the growth of the staff of the large corporation, which increases the opportunities for advancement and the so-called organisational slack which makes it possible not to work at full capacity, to have rest and recreation on the job, etc.[2]

In contrast to his predecessors, who connected the "utility" function of the corporation's internal leadership with the scale of activity or the activity growth rate, Williamson introduces two categories: 1) the level of "discretionary spending" (D), which covers all the specific utilities of the internal corporate hierarchy; and 2) profit (P). This gives the model the following form:

$$U = U(D, P).$$

The model is effected in two phases: in one phase, discretionary spending is maximised, while profit operates as the constraint; conversely, in the next phase, it is profit that is maximised, with discretionary spending operating as the constraint. The transition from one phase to another determines the peculiarities of the model structure.[3]

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[1] "The utility function of the firm undergoes occasional transformation, and this gives rise to shifts in the *modus operandi*." (Oliver E. Williamson, *op. cit.*, p. 75.)

[2] Williamson believes that "organisational slack" is not only a factor behind the growth of costs, but also a source of what he calls X-efficiency. (See: H. Leibenstein, "Allocative Efficiency versus X-Efficiency". In: *The American Economic Review*, June 1966.)

[3] The author describes his model as a dynamic stochastic model of discretionary behaviour. The dynamico-stochastic properties are introduced into the model by the assumption that the firm can select one of two positions (profit maximisa-

The following definitions of "environment" are given: H—favourable market situation (high-level condition of the environment); L—unfavourable market situation (low-level condition); M—management position maximisation; and S—stockholder position maximisation. He presents the following matrix of the probability inequalities determining the conditions for a shift from one phase to another:[1]

$$\begin{cases} P\,(L/H,\ M) > P\,(L/H,\ S) \\ P\,(H/L,\ M) < P\,(H/L,\ S). \end{cases}$$

So, in this model, the "condition of the environment" becomes a function of some properties of the system. Williamson explains that with the maximisation of "discretionary spending", opportunities

> "that the profit-maximising organisation will recognise or develop will simply go unrecognised or undeveloped if the managerial syndrome prevails".[2]

On the other hand, the basic target of the system becomes a function of the condition of the environment.

At the same time, the transition from one phase to another is based on some kind of psycho-social process which Williamson calls the "managerial

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tion), while the sequence of transitions from one set of environmental conditions to another is a simple Markov process in which the probability of transition is a function of the current state of the system. (Oliver E. Williamson, *op. cit.*, p. 76.)

[1] Williamson explains the meaning of this matrix as follows: "The probability that the system will shift to a low-level condition of the environment, given that it starts in a high-level position, will be greater if the firm adopts a managerial stance than if it is operated as a profit-maximising concern. Similarly, the probability that the system will shift to a high-level position, given that it originates in a low-level position, will be lower if the rm adopts a managerial posture." (Oliver E. Williamson, *op. cit.*, p. 77.)

[2] *Ibid.*

syndrome". The behaviour of organisations frequently demonstrates the properties of this syndrome.

> "Either the organisation is run as a 'tight ship' or is permitted to run slack. Intermediate positions are difficult to sustain. Thus, although top management might desire to restrict the exercise of discretion to activities which it controls directly, while the remainder of the organisation is run along strictly profit-maximising lines, in fact this option may be unavailable. Lower-level compliance is conditional on higher-level example."[1]

Williamson's theoretical system, like his model, is designed mainly for examining the problems of *organisation in general*. Indeed, all the basic elements of his model can be interpreted regardless of the concrete socio-economic formation, i.e. capitalism. The development of the science of large organisational systems, within whose framework Williamson has elaborated his views, is certainly of positive importance, but it is highly doubtful that such models can be used to analyse the concrete antagonisms of present-day capitalism.

It is true of the whole group of managerial theory models that their discussion of the socio-economic content of the individual model parameters is much more interesting than their purely mathematical conclusions. A discussion of this content requires, in effect, some examination of the dynamics of real and fictitious capitals underlying the large-corporation models.

The growing contradictions between real and fictitious capitals reflect the continued specialisation of the forms of capital in the development of the social division of labour. Stock capital initially operated as the only functioning capital, in contrast to loan capital. But the very form of the joint-stock

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[1] *Ibid.*, pp. 77-78.

enterprise is fraught with the possibility of an independent movement by the real capital of companies and its stockholding title. That is why with the development of the joint-stock form of ownership there has been a steady deepening of the fission of the capital-function into its real part, represented by fixed and circulating capitals of corporations, and its fictitious part, represented by the market price of corporate stock. The quantitative and qualitative discrepancy between these two parts of functioning capital is fraught with profound contradictions and conflicts.

It may appear that the capitalist company, having distributed its stock among the "public" and having obtained the funds necessary for further enlargement can afford no longer to be concerned with the way its stock capital evolves on the stock markets.

But that is not so in fact. The real being of the corporation, as represented in its balance-sheet evaluations, and its "fictitious" being, as represented in the stock-market quotations, turn out to be closely interconnected and capable of entering into a state of acute conflict.

Indeed, when issuing stock, a company undertakes the obligation of paying out dividends which are not a fixed magnitude (in the event of "common" stock, which we are here considering) but a part of the profits remaining after the payment of taxes and deductions into the undistributed profit fund, i.e. an extremely mobile and volatile magnitude. When selling its stock, the company also invests the stockholder with some rights, namely, the right to a say in deciding on the corporation's policy by voting at general meetings (but this right is valid only for the major stockholders), and the right to sell stock, which can be exercised by any stockholder, however small. The market price of stock, whose "basic" part represents the capitalisation of current dividends, also contains an extremely important component reflecting the stock-market evaluation of the general economic health of the corporation. After all, the corporation's capacity to make profits in the future depends on this.[1]

Evaluation of the prospects of profitability in the erratic capitalist economy is itself a highly nebulous task, which is made even vaguer by stock-market speculations and pressure from powerful forces seeking to "organise" the movement of stock-market prices in the desired direction. As a result, the deviation of stock-market prices from the movement of real capital may be many times greater than any possible deviations in the movement of prices from value on the commodity markets.[2]

However, the movement of stock prices is not at all a matter of indifference for the corporation which has put its stock into the stock-market "orbit". The degree of dependence differs for the various companies, but there is always some dependence, and it is mainly two-fold. First, the stock market calculates the profitability of stock not on the strength of their face value but of the existing stock-market quotation. The capitalist market, having made its own evaluation of the stock, appears to suggest that the corporation should pay dividends in accordance with its evaluation. It expects the

[1] Lenin mentioned the fact that the price of stock depended not only on current dividends, but also on the prospects of future profits, a connection which is especially enhanced in the epoch of imperialism. Remarking on the "watered" stock, i.e. inflation of the market value of stock capital as compared with the actual balance-sheet capital in the establishment of trusts, Lenin wrote: "This 'over-capitalisation' anticipated the monopoly profits..." (V. I. Lenin, *Collected Works*, Vol. 22, p. 233.)

[2] The "stock-market multiplier" gives a good idea of the extent to which stock-market prices may deviate with respect to profitability. On the New York Stock Exchange it comes to between 5 and 50. This striking discrepancy in the evaluation of various stocks per dollar of income is due to the influence exerted by monopoly groups of stock-market speculators expressing the interests of powerful investment banks and brokerage companies.

corporation to justify the hopes pinned on it by the stock market. And the corporation has to reckon with these "hopes". It has to do so, let us add, unless it wants the stock price to drop. A constantly growing stock price is a constantly growing claim on the corporation's profit, which at a point runs into acute contradiction with the corporation's need for capital of its own.

One may well ask what it is that forces the corporation to seek to maintain a high stock price which funnels off its profit?

At this point we come to the second aspect of the interdependence between the corporation and the stock price and the stock market. The stock market quotation gives the corporation a "bill of health", which it uses to lay claim to all the other types of financing by banks, insurance companies and other financial institutions.[1] The "bill of health" issued to the corporation by the stock market is in a sense the degree of confidence vested in the corporation by the top financial community. In capitalist accounting, this "good will" has a very precise quantitative expression: it is measured by the difference between the market evaluation of the issued stock capital and its balance-sheet evaluation, i.e. its face value. The good will and confidence are hard to obtain but are easy to lose, and they depend above all on the favourable disposition of the stock market, which is ruled by the big brokerage firms, and of the investment banks, which float the primary issues of securities.

The whole vast sphere of fictitious capital, including not only stock capital, but also the movement of other titles of ownership (securities, mortgages, etc.) actively caters for the economic-production process, especially the transfusion of capital, while increasingly displaying ever more

[1] "Share prices may also affect supplies of finance, not only now-issue finance but also, by permeation, borrowing-power in the bond market." (Robin Marris, *op. cit.*, p. 19.)

patent features of parasitism and super-exploitation. Real and fictitious capitals confront each other as rivals competing for profit. They also confront each other as different modes of the accumulation and transfusion of capital. It is this twofold confrontation that underlies the acute contradictions connected with the development of the corporate form of capitalist enterprise.

4. The Social Meaning of Managerial Theories

Let us bear in mind that the developing contradictions of capitalism and intricate interlacing of the struggle between classes and social groups are based on the irreconcilable interests of the bourgeoisie and the working class. Managerial theories seek to "obviate" the problem of antagonism between labour and capital by insinuating the management factor between them.

As the production system grows and becomes ever more complex, the number of career managers of every rank also grows. Evolution reflects the advancing specialisation of production and the division of labour, and the attendant enhancement of the role of coordination, which the career managers in fact undertake. But it would be basically wrong to confuse the emergence of this special professional group gradually acquiring social weight with class stratification.

Indeed, the contrast between professional managers and capitalists is an unscientific attempt to align different planes of the social structure of present-day capitalism. The formation of different and isolated professional groups under capitalism, which one finds throughout the whole of its history, does not yet amount to their class isolation. With the development of society social stratification grows and new social groups emerge: scientists and technicians, office employees (white-collar workers), etc. Bourgeois sociologists assert that stratification does away with what is left of the basic classes, which are replaced by separate "strata". But that is substituting one problem for another. The emergence and growth of new social groups has not destroyed or "eroded" the basic class antagonism of the capitalist society between the capitalists and the working class. The various groups which are formalised in social terms have a definite place with respect to the basic class division: either some of their parts are directly included in one or the other of the two basic classes, or they have an intermediate position between the two as middle strata.

The career managers have an equally multitiered position within the social structure. They have some unity as a special professional group, but this does not eliminate the class stratification within that group. While the bulk of the managers belong to the category of salaried employees, their top sections, regardless of social origin, are inevitably turned into capitalists. This occurs for various concrete reasons: the big capitalists' concern to have the goals of the senior managers tied to their own goals, managers' use of their status for the purpose of personal enrichment, etc. But whatever the concrete reasons for the conversion of the senior managers into capitalists, the social laws of capital create the general background against which this conversion actually takes place. In virtue of these laws, any important position in society is "capitalised", is converted into capital.

Under present-day capitalism, large fortunes are invested in stocks, bonds and other titles of ownership. The personal fortunes, laying claim to a flow of earnings now and in the future, are converted into capital, a self-proliferating value.

The career manager, who according to the theory of the managerial revolution allegedly opposes the capitalist owner, inevitably turns into a capitalist.

That is the basis on which a highly important process goes forward under present-day capitalism: in the large corporation there is not only a constant separation of ownership from management, but also simultaneously and parallel with it the opposite process, in which management and ownership are reunited as the senior executives turn into capitalists. That is the aspect of the matter that the theorists of the managerial revolution want to obscure, for which purpose they absolutise one line of development and ignore the other.

In the period of major organisational changes and feverish financial activity in the capitalist countries, the greatest attention is attracted by the nouveaux riches, the men who started out with a small business, rapidly developed it into a big one, and made large fortunes. The tremendous scale of the mergers in the United States and West European countries in the 1960s brought to the surface people like J. Ling in the United States, who built up the sprawling conglomerate Ling-Temco-Vought, Inc. and who had started out after the Second World War as the owner of a small repair shop: or William Stater in Britain, who built up one of the biggest British conglomerates, Stater-Walker Securities Ltd., and who had also started out as a small-time financial dealer.

But others who are not so much in the limelight, but who are as powerful and rich, also rise to the surface. Thus, in contrast to Ling, a career manager named A. Jennings started out in ITT as a salaried employee. In a relatively short time, he created an empire ranking eleventh among the 500 major industrial corporations of the United States, and became its powerful head and co-owner. Weinstock, a British manager, provides another similar example. An economist and a Fellow of the Statistical Society, he joined the British General Electric Company as a manager when it was in financial straits. In a short period (1967-68), he brought about the merger of three large firms and set up an electrical engineering company that is one of the biggest in Europe. He became its chief executive while simultaneously amassing a multimillion personal fortune.[1]

There are many such examples. The rise of managers and their simultaneous conversion into major capitalists is a characteristic phenomenon of present-day capitalism connected with the scientific and technical revolution and the sharpening competition between the monopolies on a world-wide scale.

What has the current development of capitalism left of Bernham's "managerial revolution"? There is good reason to say that it lies in ruins. In fact, it could be ignored, but for the fact that this theory reflects (in a veiled form) important social processes linked with the development of capitalism's economic contradictions. That is why it is interesting to look at how this theory is being dismantled in bourgeois writings.

Larner uses the term managerial revolution in quotes, because he believes that it is unscientific. Larner asks this question: where does the dividing line between the "managerial" and the "family" firm run? His formulation of the problem is traditional, but his answer contains some new approaches. He writes:

> "The classification system used describes not *who* controls our largest corporations but rather *how* or by what means (stock ownership or position in management) these corporations are controlled."

To explain his idea he shows how corporations are included in this or that group, and adds:

> "Five companies...which are classified as management controlled appear to be controlled, or at least strongly influenced, by a single

[1] See: Anthony Vice, *The Strategy of Takeovers*, McGraw-Hill Book Company, London, 1971, p. 12.

> family within their management. Yet these families owned only a very small fraction of the outstanding voting stock. The five companies and their controlling families are: IBM (Watson), Inland Steel (Block), Weyerhaeuser (Weyerhaeuser), Federated Department Stores (Lazarus), and J. F. Stevens (Stevens)."[1]

So, the author recognises that the management and the capital factor are interconnected and parallel with each other. But the important thing for him is to clarify the basis of power: is it a strategic position in management or ownership of capital? Since he does not contrast capital and ownership with management, his approach helps to clarify highly important distinctions *within* the big corporate bourgeoisie. But the author stops short of doing so. His book is a critique of the "managerial revolution" from neoclassical positions. We have already established that it is not right to "obviate" the contradictions within the large firm in such a way. But ahead lies this problem: to establish the kind of distinctions that are of essential importance in aggravating the contradictions of capitalism which can be seen in the orientation of different groups of the bourgeoisie. That is the line social research should take in order to expose the "managerial revolution" theory. The point is that the reassertion of the idea concerning the total unity of the career managers and the capitalist stockholders is just as unproductive as their absolute contraposition.

The British analyst T. Nichols, who admits that his views were developed in the Marxist tradition, takes an approach that is much more historical and consistent. He writes:

> "In the century since the joint stock company was introduced the hired manager has gained in status. His power has increased along with

[1] R. Larner, *op. cit.*, p. 19.

that of the corporation. His social relations with stockholders and propertied directors are unquestionably more likely to be on terms of social equality. But, *de jure*, his function is still to serve the shareholder interest and, in practice, there is little reason to suppose that his outlook is much different from that of propertied directors. ...The norms which govern his conduct derive in part from the shareholder interest and ... his position approximates to that of the propertied director. Managerialists have written of a '*divorce*' or 'separation' of ownership and control. In this context we find it more fitting to write of a 'marriage of convenience."[1]

So, the "managerial revolution" has come full circle. The total domination by the managerial "class" has given way either to their total unity with capital or to a "marriage of convenience", a very apt phrase used by Nichols to reflect the relations between the mass of managers and the capitalists. But I shall try to approach the matter from a different angle.

The relationships within the corporate hierarchy suggest that there are differently oriented groups within the big bourgeoisie connected with the activity of monopoly corporations. This difference in orientation, for its part, is closely connected with the different movement of real and fictitious capital, as described above. The contradictory development of the socio-economic processes stemming from the growth of the large corporation constantly brings out the existence of two bourgeois groups. One of them stakes on the growing autonomy of the large corporation, while the other is connected with the movement of fictitious capital, with the stock market, with the world of "high finance". The difference

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[1] Theo Nichols. *Ownership, Control and Ideology*, George Allen and Unwin Ltd., London, 1969, p. 141.

between these two groups is not at all absolute; it is mobile, changing in time and from one corporation to another. Besides, this distinction is mostly covert, being overshadowed by the class solidarity of the big bourgeoisie in face of the basic class antagonism with the working class. But from time to time the operation of the in-depth contradictions arising from the capitalist mode of socialisation of production, with concentration and monopolisation, brings to the surface the different orientations of the groups of the big bourgeoisie, making this distinction acute and conflicting.

In order to clarify this important matter, let us look at the mergers and takeovers in the developed capitalist countries in the 1960s and early 1970s. Because of the scale and depth of this process in some countries it can be regarded as an important restructuring of the organisational forms of capital. In the United States, the centralisation of capital in the 1960s has been called "the third big wave of mergers". US economists have estimated that all these mergers summed up to 21.1 per cent of total manufacturing and mining assets (as compared to 16.3 per cent of the "total disappearance" of independent assets from 1921 to 1931.[1]

The scale of mergers in Britain will be seen from the following data: in the 1950*s*, 10 per cent of quoted company funds went on acquisitions; between 1960 and 1965, this figure averaged 16 per cent, culminating in 1968, when the proportion of the total flow of company funds devoted to acquisitions reached the unprecedented figure of about one-third.[2] The mergers resulted in the accelerated concentration of capital. Thus, measured as the share of 100 biggest companies in manufacturing output, the pace of concentration in the 1960s trebled as compared with the preceding period:

[1] *The American Economic Review*, May 1971, No. 2, p. 105.
[2] Anthony Vice, *op. cit.*, p. XV.

every year the share increased by one percentage point, as compared with the three years it used to take to achieve such growth before. By 1970, the 100 biggest companies in Britain accounted for 55 per cent of industrial output.[1]

The concentration of capital was equally impressive in West European countries. According to some estimates, the share of the 50 biggest monopolies in the gross domestic product of the EEC countries went up from 35 per cent in 1960 to nearly 46 per cent in 1970, this growth being closely connected with the intensive process of major mergers which swept Western Europe in the 1960s.[2]

So, the wave of mergers in the 1960s rolled across the whole capitalist world and was unusually sweeping. The centralisation of capital brought out some essential distinctions between companies effecting the mergers and companies accepting the merger offer. These distinctions were characterised in different ways, but they were aimed to bring out one key point of difference, namely, the orientation of the various companies and their management with respect to the stock market and external sources of finance.

It is a curious fact that the greatest scope of the mergers went hand in hand with a loud propaganda campaign on the part of the ideologists and the actual organisers of the mergers in defence of the "small stockholder", who was presented as a victim of powerful companies under the control of egoistic and inefficient management.[3]

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[1] *The Banker*, July 1973, pp. 758-760.

[2] *European Economic Review*, Vol. 4, No. 4, December 1973, p. 394.

[3] Here is what, for instance, James Ling, the head of a major conglomerate, said in response to a threat of the US Department of Justice to limit the possibility of takeovers through the stock market: "Today, in the United States there are essentially two types of corporate management: (a) the professional caretakers who seek prestige, job security, a weekly paycheck, and good fellowship with their cohorts in other companies, overspending time and other corporate re-

Let us recall that these "entrepreneurial innovators" were the ones who started the feverish speculation and inflated stock prices and prepared the stock-market collapses in 1970 and 1974, so pocketing the savings of millions of small stockholders whom they claim to champion.

The process of mergers in the 1960s and early 1970s in the developed capitalist countries marked an important turning point in the development of the trend which had been in evidence for several decades before that, the trend towards a growing autonomy of the large corporations from the stock market, and greater independence in the movement of real capital relative to its fictitious embodiment. The revival of the stock market and the whole sphere of fictitious capital sprang from the basic requirements of capitalist production. The closed structure of the large corporations, taking shape over the decades, ran into acute conflict with the need to shift vast masses of capital from the old industries into the new. The old methods of financing monopoly expansion in the new industries proved to be inadequate. The merger process, which ran in close connection with the enlivened role of the stock market and the whole sphere of fictitious capital, was a purely capitalist way of solving the problem of the flow of capital into the most modern sectors of the economy.

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sources, and (b) the entrepreneurial innovators who seek challenges, increasing values for their shareholders, and who are willing to put their futures on the line through equity participation in their companies." (Stanley H. Brown, *Ling. The Rise, Fall and Return of a Texas Titan*, Atheneum, New York, 1972, pp. 154-155.)

CHAPTER ELEVEN

THE CONCEPT OF "HUMAN CAPITAL"

1. Theoretical Premises

Up until recently, Western economists paid little attention to problems relating to the *formation* of labour power, concentrating on the *use* of manpower resources. But the scientific and technical revolution raised a host of problems connected with the *formation* of qualitatively new labour power. The structural changes in the economy of present-day capitalism provided the objective basis for the emergence of the theory of "human capital". The immediate intellectual impulse to its formulation was given by works analysing the problems of economic growth.[1] These works brought out the vast role played in economic growth by qualitative changes in labour, undermining the traditional assumption of the production factor theory that all the factors were qualitatively homogeneous. Having noted the distinctions in the quality of one of these factors, labour, bourgeois economists logically went on to analyse the reasons of its intrinsic heterogeneity and turned to such phenomena as

[1] See, for instance, Gary S. Becker, *Human Capital. A Theoretical and Empirical Analysis, with Special Reference to Education,* Columbia University Press, New York, 1964, p. 1.

education, accumulation of production experience, and so on, which became the object of research in the concept of "human capital".

That concept was formulated in the late 1950s and early 1960s, primarily by the well-known US economists Gary S. Becker, Burton A. Weisbrod, Jacob Mincer, Lee W. Hansen, Theodore W. Schultz. Later on, contributions to it were made by Samuel Bowles, Yoram Weiss, Yoram Ben-Porath, Finis Welch, Barry R. Chiswick, and others.

The "human capital" concept has on the whole developed along neoclassical lines. Its advocates, however, use the analytical instruments of the neoclassical school to study the social institutions (education, health care, etc.) which economists rarely analysed in the past. The emphasis here is on quantitative analysis, while institutional factors which are hard to quantify (like the role of trade unions) are relegated into the background.

As it was already pointed out, up until recently bourgeois economists paid only sporadic attention to the *formation of labour power*: they lacked the analytical instruments for studying the process. In these conditions, they naturally turned to that section of economic theory which analysed the *formation of capital* and borrowed from it many important elements of the conceptual apparatus. The proposition that these two formative processes are analogous lies at the root of the "human capital" theory. This is expressed in its very title. "Human capital" implies man's knowledge, skills and abilities which enhance the productive power of his labour:

> "It is a form of capital because it is the source of future earnings, or of future satisfactions, or of both of them. It is *human* because it is an integral part of man."[1]

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[1] Theodore W. Schultz, "Human Capital: Policy Issues and Research Opportunities". In: *Human Resources*,

Education, occupational training, medical care, migration, search for information on prices and incomes, and the bearing and raising of children are seen as the major forms of human investment. Education and occupational training increase the individual's knowledge, that is, the *volume* of "human capital"; health care lengthens its *service life* by reducing the incidence of disease and the death rate; migration and search for information help to move manpower into regions and sectors where payment for work is higher, that is, raise the *price* of the services rendered by "human capital"; the bearing and raising of children reproduce "human capital" in the *next generation.*

It is easy to see that all the factors classified as "investment in human capital" are elements of the reproduction of labour power. But such a classification is incomplete and lacks system: it is incomplete because the value of labour power also depends on many other factors, primarily on the value of the resources necessary to maintain the worker "in his normal state as a labouring individual"[1]; it lacks system, because education, health care, migration, and search for information relate to different stages in the reproduction of labour power and have a different influence on its value and price.

Education and health care are factors that have a long-term influence. Education produces qualitatively new, higher-skilled labour power capable of doing more complex work, and health care enables the individual to work longer and more intensively. In contrast to these, migration and search for information are short-term factors. Education and health care entail a real increase in the value of labour power, whereas migration and search for information reflect the fluctuations of the price of labour power round its value. Migration and search

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Fiftieth Anniversary Colloquium VI. National Bureau of Economic Research, New York, 1972, p. 5.

[1] Karl Marx, *Capital*, Vol. I, p. 168.

for information are distributive processes, whereas education and health care are elements of the reproduction of labour power. Bourgeois authors see the formulation of the concept of "human capital" as a major theoretical advance, and the US economist Mary Bowman has even described it as a "revolution in economic thought".[1]

In actual fact, there is nothing new about the idea that human knowledge and abilities are similar to physical capital; in one form or another, it has always been among the instruments of economic analysis. Thus, Adam Smith wrote:

> "The improved dexterity of a workman may be considered in the same light as a machine or instrument of trade which facilitates and abridges labour, and which, though it costs a certain expence, repays that expence with a profit."[2]

How justified is that analogy? Is there a germ of truth in the comparison?

As an analytical device, a comparison between the formation of labour power and that of the material means of production is well justified. Marx himself used such a method of analysis in his *Capital* when trying to clarify, for instance, the different roles of constant and variable capital in the creation of value. This is a fruitful comparison, for it helps to bring out the specifics of the phenomena being considered. Moreover, from the standpoint

[1] See: Mary J. Bowman, "The Human Investment Revolution in Economic Thought". In: *Sociology of Education*, Spring 1966, Vol. 39, No. 2, pp. 111-137. Another economist wrote: "The concept of human capital constitutes a major advance in economic analysis. Human capital makes it easy to apply the analytical framework that has been developed for physical investment to human investment." (Lester C. Thurow, *Investment in Human Capital*, Wadsworth Publishing Company, Inc., Belmont, California, 1970, p. 121.)

[2] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, Vol. 1, Methuen and Co., Ltd., London, 1950, p. 265.

of the production process as such, the development of human abilities

> "can be seen as the production of *fixed capital*, this fixed capital being man himself".[1]

But comparing two things does not mean identifying them, for comparison implies the need to pinpoint the attributes of each of the objects being compared.

That is what the advocates of the "human capital" theory fail to take into account, for they absolutise the similarities to the detriment of the distinctions. True, some Western economists also admit that the analogy between physical and "human" capital is limited and draw up a fairly long list of dissimilarities between the two forms of capital. They maintain, for instance, that "human capital" differs from physical capital in the degree of liquidity.[2] The investment period for physical capital (18-24 months on average) is much shorter as compared with that for "human capital". Education can last from 12 to 20 years. The degree of risk and uncertainty in educational investment is greater than it is in "conventional" capital investments, and so forth.

The list can be continued, but all these distinctions are of a technical nature: they somewhat modify the conventional procedure in investment decisions, but do not fundamentally separate physical capital from "human capital".

In fact, the economic nature of physical and "human" capital (that is, of the means of production and labour power) is fundamentally different. "Human capital" creates value, while physical capital

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[1] Karl Marx, *Grundrisse der Kritik der Politischen Ökonomie*, Foreign Languages Publishing House, Moscow, 1939, p. 599.

[2] "The most critical attribute of human capital arises from the fact that the person and his human capital are inseparable." (Theodore W. Schultz, *op. cit.*, p. 8.)

transfers it; the former is the object of exploitation, and the latter, its instrument. The value potentialities of the means of production are strictly limited, for these are capable only of transferring the value embodied in them. Marx wrote:

> "Insofar as the instrument of production is itself a value, embodied labour, *it does not introduce anything as a productive force.*"[1]

Man, on the other hand, is capable of creating a greater value than that which goes into the reproduction of his labour power, including his training. "Human capital" (i.e. the working man's knowledge and abilities) can be realised only in his own labour; the value of capital, on the other hand, can grow without any labour imputs on the part of its owner.

Marx noted this distinction in criticising the theories in which labour power was seen as capital. He wrote:

> "Wages are conceived here as interest, and therefore labour-power as the capital yielding this interest. For example, if the wage for one year amounts to £50 and the rate of interest is 5%, the annual labour-power is equal to a capital of £1,000. The insanity of the capitalist mode of conception reaches its climax here, for instead of explaining the expansion of capital on the basis of the exploitation of labour-power, the matter is reversed and the productivity of labour-power is explained by attributing this mystical quality of interest-bearing capital to labour-power itself.
> ...Unfortunately two disagreeably frustrating facts mar this thoughtless conception. In the first place, the labourer must work in order to obtain this interest. In the second place, he cannot transform the capital-value of his

[1] Karl Marx, *Grundrisse der Kritik der Politischen Ökonomie*, p. 651.

> labour-power into cash by transferring it. Rather, the annual value of his labour-power is equal to his average annual wage, and what he has to give the buyer in return through his labour is this same value plus a surplus-value, i.e., the increment added by his labour."[1]

Western economists ignore the fact that capital is not just a "store of wealth", but a definite social relationship taking shape with respect to that "store". The purely technical approach, when investments are spelled out as any expenditures that entail a foregoing of current consumption for the sake of future benefits, invites the conclusion that "human capital" is identical with physical capital.

If an individual's growing educational level enables him to obtain an additional income over and above the cost of the education, the educational expenses can be described as expanding value. But to say that it is capital, that is, self-expanding value would, I think, be absurd. The value of an individual's skills does not expand of its own accord: an indispensable condition here is the labour of its vehicle. The accumulation of knowledge and skills is

> "the most important result of antecedent labour; its form of existence, however, is living labour itself."[2]

Western economists overlook the fact that property in the means of production implies not only ownership of a definite "store of capital goods", but also economic power over those who have no such "store". Marx wrote:

> "Capitalist production ... of itself reproduces the separation between labour-power

[1] Karl Marx, *Capital*, Vol. III, pp. 465-466.
[2] Karl Marx, *Theories of Surplus-Value*, Part III, Progress Publishers, Moscow, 1975, p. 295.

and the means of labour. It thereby reproduces and perpetuates the condition for exploiting the labourer. It incessantly forces him to sell his labour-power in order to live, and enables the capitalist to purchase labour-power in order that he may enrich himself."[1]

In contrast to property in the means of production, possession of definite skills does not entail the exploitation of other individuals' wage labour, it does not imply relations of control and subordination, and consequently, the idea that human abilities are capital leads to a distorted picture of the intrinsic nature of the capitalist mode of production.

But while differing in their *politico-economic* content, the formation of capital and the formation of labour power have definite *techno-economic similarities*: both call for the diversion of sizable resources at the expense of current consumption, both determine the future development level of the economy, and both have a long-term effect on production. The broad interpretation of the category of "capital" by present-day Western economists goes back to the theory of the US researcher Irving Fisher, who saw capital as any "store of wealth" existing at a given moment of time. Fisher contrasted capital with income, which he defined as a "flow of wealth" over a definite period.

From that standpoint, the formulation of the "human capital" concept amounted to no more than recognition that human skills and abilities can be a "store", that is, can be *accumulated*. In other words, bourgeois economics has in effect rediscovered something that Smith and Ricardo already knew and to which Marx repeatedly referred.[2]

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[1] Karl Marx, *Capital*, p. 541.

[2] "The reproduction of the working class carries with it the accumulation of skill, that is handed down from one generation to another." (Karl Marx, *Capital*, Vol. I, p. 538.)

Soviet economists have elaborated these ideas. See, for

So, the idea of "human capital" in bourgeois economics has a two-fold purpose. On the one hand, it has a distinct ideological edge, and on the other, the very fact that Western economists resorted to that idea reflected their attempts to take into account the actual changes in the economy, whose substance is that the accumulation of the non-material elements of wealth is now of paramount importance for the whole course of social reproduction.

2. Efficiency of "Investment in Human Capital"

When the concept of "human capital" was formulated, numerous attempts were made to measure its volume and economic efficiency. This aspect is of some practical interest. Economists estimate efficiency by comparing the cost of "investment in human capital" with the income it yields, using the techniques of "cost and benefit" analysis.

The research is carried out in three stages: (A) Identification of benefits and their evaluation (with a view to the time factor); (B) Identification of costs and their evaluation (also with a view to the time factor); and (C) Comparison of discounted costs and benefits. In studying the profitability of investment in "human capital", attention was focussed on formal education, and we shall now go on to consider assessments of its efficiency.

(A) Education influences the individual's money income.[1] According to the theorists of "human capi-

instance, V. I. Martsinkevich, *Education in the USA: Economic Significance and Efficiency*, Moscow, 1967; G. E. Skorov, *The Developing Countries: Education, Employment and Economic Growth*, Moscow, 1971; also his: *Socialist Accumulation. Questions of Theory and Planning*, Moscow, 1973 (all in Russian).

[1] According to this view, apart from the direct advantages accruing to the individual from education, it also engenders various "external" benefits which are enjoyed by third persons or by society as a whole, but it is very difficult

tal", education makes the individual's labour more productive, and this serves to increase his wages. Consequently, the task is to calculate the contribution of education to wage growth. So, the wage of a working person with a definite educational level consists of two basic parts: first, the income he would have received with zero education, and second, the income from educational investment:

$$Y_n = X_0 + rC_n,$$

where Y_n is the income of a person with n years of education; X_0—the income of a person with zero education; C_n—the volume of investments over n years of education, i.e. the accumulated "human capital"; and r—returns on educational investment.

The theorists of "human capital" regard wages as a stratified structure, where every "stratum" is related to a definite educational level. The "stratum" of income that relates to a given educational level represents the money income from investments in that education. Thus, the money income from higher education can be roughly defined as the difference between the lifetime income of two persons: one of these with a higher education, and the other, with a secondary education. *Table 1* (see p. 502) shows the additional lifetime income from a higher educational level.

An evaluation of the economic returns from education is of real economic importance. As education levels rise, the value of labour power increases, for the production and reproduction of higher-skilled labour power calls for a greater sum-total of values. But an increase in income as the result of growing educational levels is only one aspect of the problem. The complexification of labour entails changes in the value not only of the necessary, but

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to make a quantitative evaluation of these external effects. (See: Burton A. Weisbrod, "Education and Investment in Human Capital". In: *The Journal of Political Economy*, Vol. 70, 1962, No. 5, pp. 106-123.)

also of the surplus product. The connection between the quality of labour power and the production of surplus value is an important and complex problem. It has to be studied separately, but "human capital" theorists have not considered it at all.

(B) Besides direct outlays on education, "human capital" theorists also include in the cost of education the student's "forgone income", that is, the

Table 1

Additional Income of Persons with Different Educational Levels in the USA*, 1972 (dollars)

Eight years of elementary school		Additional income as compared with the income of persons with eight years of elementary school
High school:	1 to 3 years	45,500
	4 years	135,100
College:	1 to 3 years	199,700
	4 years	366,800

* Men over 18 years of age.

Source: *US Bureau of the Census*, *Current Population Reports*, Series P-60, No. 92, p. 22.

income he fails to receive because during the educational period he is not employed in production. Many bourgeois economists came out sharply against the inclusion of "forgone income" in the costs of education, regarding it as fictitious. Indeed, in contrast, say, to the outlays on teachers' pay or on the maintenance of educational facilities, forgone income does not exist in the form of a real sum of money that goes into education. But if a student is to acquire the necessary knowledge, he has to make labour inputs in the course of the educational process, and these labour inputs are not fictitious, but quite real; although they are not taken into account in the computation of the national income, they undoubtedly help to increase the national wealth.

It is as yet impossible to measure the students' actual labour contribution to the production of their skills, for one has to know their actual "working hours", the intensiveness of their work, and the degree of its complexity. Since there are no natural indicators directly measuring labour in education, we think that forgone income could be adopted as a tentative measure of its value.[1]

(C) At the final stage of "cost-benefit" analysis, costs are compared with benefits. But first these magnitudes have to be discounted. However, it is hard to decide what rate of interest should be chosen as the discount coefficient. That is why the most popular method now is to calculate the "internal rate of return", that is, the interest rate at which the discounted value of future benefits equals the discounted value of costs:

$$\sum_{t=0}^{n} \frac{B_t}{(1+r)^t} = \sum_{t=0}^{n} \frac{C_t}{(1+r)^t},$$

where B_t is income from education at the given time t; C_t—educational costs at the given time t; n—number of periods of time; and r—internal rate of return (the higher this rate, the more profitable is the investment in education).

Table 2 (see p. 504) shows the estimated rates of return on complete high school and college education in the United States.

The educational efficiency estimates calculated with the help of rates of return are open to criticism in many respects. Thus, they do not take

[1] In computing the total cost of education in the USSR, some Soviet economists take into account the income forgone in the educational period (see, for instance, L. I. Tulchinsky, *Financial Problems of Occupational Education in the USSR*, Moscow, 1968, in Russian).

into account the influence exerted on income by many factors, like the quality of education, personal abilities, etc.

But the main omission of the "human capital" theory is that it ignores the working individual's

Table 2

Estimated Rates of Return on Complete High School and College Education in the USA (per cent)

Author	Year of publication	Year to which estimate applies	Rate of return	
			high school	college
Becker	1964	1938	16.0	14.5
Carnoy Marenbach	1975	1939	12.5	11.0
Becker	1964	1949	20.0	13.0
Hansen	1963	1949	15.3	11.6
Carnoy Marenbach	1975	1949	22.7	13.2
Schultz	1961	1958	10.0	11.0
Becker	1964	1958	28.0	14.8
Hynes	1970	1959	19.5	13.6
Frieman	1975	1959	—	11.0
Carnoy Marenbach	1975	1969	14.6	17.6
Frieman	1975	1969	—	11.5
Carnoy Marenbach	1975	1969	18.8	15.4
Frieman	1975	1974	—	8.5

Sources: *Revue d'Economie Politique*, 1973, No. 3, p. 413; L. Becker, *Human Capital*, New York, 1964, p. 128; *The Journal of Human Resources*, 1975, Vol. 10, No. 3, pp. 296, 316.

occupation: the occupational structure is the mediating link between the educational and production structures. How does this "transmission mechanism" function? What is the connection between changes in the educational level of labour power and changes in its occupational structure? Will every rise in educational level always entail changes in the working person's occupational status and his remuneration? These questions have, in effect, escaped the notice of "human capital" theorists.

Finally, estimates based on differences in wage levels without regard for differences in output can grossly distort the actual economic effect of education and occupational training.

A point to note is that in the "human capital" concept the internal rate of return is seen not only as an *indicator* of the effectiveness of educational costs, but also as a *regulator* of the distribution of investments between different types and levels of education, and also between the whole educational system and the entire economy. The advocates of that concept maintain that the volume of investments in one sphere of the economy or another should be determined by the priorities established in accordance with the rate of return. High rates indicate underinvestment in the given industry or sphere of the economy, and low rates, overinvestment. That is why optimal distribution of resources will ensure equal rates of return on every type of investment.

Western economists draw an analogy between the rate of return on "human capital" and conventional rate of profit. That is why they see the choice of the type and level of education as adoption of an investment decision. To decide the question of whether to continue his education, an individual should compare the expected rate of return with the rate of interest.[1] Students, "human capital" theorists say, are guided by the same motive as entrepre-

[1] "An education will be purchased if the expected rate of return exceeds the rate of interest. The education will not be purchased if the interest rate exceeds the rate of return." (Robert Campbell and Berry N. Siegel, "The Demand for Higher Education in the United States. 1919-1964". In: *The American Economic Review*, June 1967, Vol. 57, No. 3, p. 483.)

neurs, that is, profit maximisation, investing their resources in order to obtain the highest rate of return.[1]

But the attempt to present the internal rate of return as a regulator of educational investments invites serious objections.

First, the urge to obtain the largest money income should not be seen as the only incentive to education. Education is also chosen for various other, non-pecuniary reasons, like prestige, creativity, etc. The money-oriented economic model of education can be used only as an abstraction of the most general order, as a first approximation to reality.

Second, there is no analysis of the interrelationship between the choice of educational level and the choice of occupation. What comes first: the choice of occupation or that of educational level? If individuals choose occupations (i.e. types of education), there is hardly any sense in calculating rates of return for different educational levels. Moreover, in choosing an education, individuals can be guided by totally different motives than in choosing an occupation. Western researchers differ widely on these issues.

The third and most important point of all is that the very mechanism for regulating investments in education differs from the one described in the "human capital" concept. People strive towards an education not because they see it as a profitable investment, but because education enables them to sell their labour power. For a working person, education has now become an economic necessity. Without a definite level of training, a working person can be left out of production altogether.

[1] "I treat college students as firms, behaving as entrepreneurs in allocating their own time and their other resources in investing in themselves." (Theodore W. Schultz, "Optimal Investment in College Instruction: Equity and Efficiency". In: *The Journal of Political Economy*, Vol. 80, No. 3, part II, May-June 1972, p. 2.)

"Human capital" theorists maintain that the volume of investments in education is determined by the "economic attractiveness" of these investments for the working person, by the "internal rate of return". But this would have been so only if all the working people had sufficient resources to "purchase" an education of any level. An individual without such resources can purchase only as much education as his and his family's material condition will allow. So, what regulates investments in education is not so much the degree of their *profitability* as the *possibility* of such investments, which ultimately depends on the requirements of capital in trained labour power. When these requirements grow, the working people are enabled to raise their educational standards. As Engels noted, the bourgeoisie bestows upon the workers "only so much education as lies in the interest of the bourgeoisie".[1] The working people are given access to higher stages of education only when this is necessary for the normal functioning of social capital. It is only when the capitalist class is obliged to sanction some requirement as a socially necessary one that the working class is enabled to satisfy that requirement.

From the standpoint of the capitalist, the educational expenditures of the aggregate worker (in so far as these reduce surplus value and increase the value of labour power) should be seen as profit-yielding investments. The reduction of surplus value here is temporary and is eventually recouped, since higher-skilled labour power is capable of more sophisticated work, and the latter produces more surplus value than simple work.[2]

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[1] Karl Marx and Frederick Engels, *Collected Works*, Vol. 4, p. 407.

[2] "All labour of a higher or more complicated character than average labour is expenditure of labour-power of a more costly kind, labour-power whose production has cost more time and labour, and which therefore has a higher value than unskilled or simple labour-power. This power

That is why entrepreneurs have an economic stake in raising the quality of wage labour.[1]

Consequently, the mechanism regulating the allocation of educational investments is very different from what the "human capital" theorists imagine it to be. In the final count, the *economic* impulse to education does not proceed from those who purchase it, or (to use a term applied by "human capital" theorists) from the "investors in human capital", but from the capitalist class.[2] Under capitalism, investments into this or that industry are regulated by the rate of profit. Educational investments depend on the requirements of social capital in trained labour power, that is, they are ultimately determined by the capitalists' drive for profit. The difference is that the bulk of investments in education is not made by individual entrepreneurs, but by the capitalist class as a whole. So, the "profitability" of education for the students themselves can regulate educational expenditures only up to a point, namely, so long as the cost of a definite type and level of education does not exceed the resources that the future worker or his family can set aside for this purpose.

The rate of return does not explain why entrepreneurs agree to pay higher wages for skilled labour. Focussing their analysis on the supply of edu-

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being of higher value, its consumption is labour of a higher class, labour that creates in equal times proportionally higher values than unskilled labour does." (Karl Marx, *Capital*, Vol. I, pp. 191-192.)

[1] According to the Soviet economist V. Martsinkevich, in the early 1960s, the coefficient for labour of average complexity in the US economy was 1.7, i.e., almost twice as much value was produced in an hour than would have been produced solely with simple labour. (V. Martsinkevich, *op. cit.*, p. 158.)

[2] One should also bear in mind various social, political and other factors. It is obvious, for instance, that the proletariat's class struggle under capitalism is a major motive force in raising the educational standards of aggregate labour power.

cated labour power, the advocates of the "human capital" concept have virtually neglected the problem of demand for such labour power. That is one of the most vulnerable points of the "human capital" theory. The fact that better educated people usually receive higher incomes is simply taken for granted. But without understanding the economic effect of education and training of personnel for the entrepreneurs, one can never explain the structure of incomes or the structure of the distribution of labour power itself according to educational and skill standards. I think that Marx's teaching on complex labour can provide a fruitful basis for analysing these economic phenomena.

3. "Human Capital" Theory and Distribution

The "distributive" aspect of the "human capital" theory has to be specially considered. In the past, bourgeois economists concentrated on so-called functional distribution, that is, the distribution of income by factors of production: labour, land and capital. The "human capital" concept introduced a fourth factor—"human capital"—and shifted the emphasis to *personal* distribution of income.

Using regressional analysis, bourgeois economists determine the contribution of this or that factor to the growth of wages. The results they obtain are often most contradictory. Thus, differences in educational standards serve to explain from 8 to 75 per cent of the wage differentials. Efforts are also being made to separate the influence of education on wages from the influence of personal abilities. The well-known US economist Edward F. Denison initially attributed 40 per cent of the difference in the incomes of persons with different educational standards to unequal abilities,[1] but later works usually give a lower figure: 10-25 per cent.

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[1] Edward F. Denison, "*The Sources of Economic Growth in the United States and the Alternatives Before Us*". A Sup-

Use of the multiple correlation method runs into econometric difficulties.[1] Since the samples used by researchers in this field are not representative enough, some of their qualitative indicators are indeterminate and the models themselves are more or less tentative, the cognitive value of their results is reduced.

As for practical recommendations in economic and social policy, "human capital" theorists advocate outlays on education not only as highly efficient investments, but also as a major instrument in redistributing income. Like the 19th century US educator Horace Mann, bourgeois economists call education "the great equaliser". They believe that if "human capital" grows faster than the material means of production, this leads to a more even distribution of personal income:

> "Since the distribution of personal income from non-human capital (income-producing property) is much more unequal than that from human capital, and as the stock of human capital increases relative to that of non-human capital, other things being equal, the inequality in the distribution of personal income is thereby reduced."[2]

These hopes, however, are not borne out by reality.

Table 3 (see p. 512) shows the distribution of money income depending on the educational level among adult white males in the United States (i.e. the category of labour power for which internal rates of return

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plementary Paper of the Committee for Economic Development, New York, 1972, pp. 69-70.

[1] See: Stephen Merrett, "The Rate of Return to Education: A Critique". In: *Oxford Economic Papers*, Vol. 18, November 1966, No. 3, pp. 289-303.

[2] Theodore W. Schultz, "Human Capital: Policy Issues and Research Opportunities". In: *Human Resources*, Fiftieth Anniversary Colloquium VI. National Bureau of Economic Research, New York, 1972, p. 25.

are most often calculated). The figures show that although from 1950 to 1970 the educational inequality among white males was somewhat reduced, the inequality in money income increased, and this is at odds with the assertions of "human capital" theorists. To explain this phenomenon, let us turn to the Marxist category of simple labour. The standard of training of simple labour is a critical, "threshold" magnitude, and the attainment of such a standard is something of a permit for joining the regular army of wage labour. That is why even if the inequality in terms of educational man-years is somewhat reduced, the inequality in education above the threshold level remains the same, and there is no reason to expect a reduction in the inequality of income.

Under capitalism, the educational system itself breeds discrimination and social injustice. Far from being a "great equaliser", it is one of the channels for passing on the inequality from one generation to another. As for the structure of income distribution, it cannot be explained without analysing the distribution of capital, the initial cause of the economic inequality in capitalist society, and without analysing the balance of class forces in the given historical period.

In this respect, the "human capital" theory may be seen as yet another version of the idea on the "transformation of capitalism". According to this version, the "regeneration" of the capitalist system does not mean that economic power is taken over by a new social stratum—the managers (as in the "managerial revolution" theory) or the technostructure (as in Galbraith's theory of the "new industrial society")—or that property is diffused (as in the theory of "people's capitalism"). Its exponents say that capitalism changes its social nature as a new group of capitalists—the owners of "human capital"—emerges alongside the owners of the means of production:

"... Labourers have become capitalists in the sense that they have acquired much knowledge and many skills that have economic value."[1]

In other words, capitalist society allegedly no longer consists of two antagonistic classes—the proletariat and the bourgeoisie—but of two more

Table 3

Education and Money Income among Adult White Males in the USA (per cent)

Distribution of white males by groups (quintiles)*	Share of each group in the total number of educational man-years		Share of each group in total money income	
	1950	1970	1950	1970
Highest	31.1	29.3	44.8	46.3
Second	24.9	22.3	23.7	25.0
Third	19.0	21.3	17.5	16.7
Fourth	16.4	16.4	10.9	9.4
Lowest	8.6	10.7	3.2	2.6

* Each group contains 20 per cent of the total number of white males.

Source: L. Thurow, "Measuring the Economic Benefits of Education". In: *Higher Education and the Labor Market*, New York, 1974, p. 385.

or less similar groups of capitalists. These two groups can compete with each other, but their fundamental interests are allegedly identical.

In fact, however, in spite of the growing educational standards of the aggregate labour force, the proletarian is still a proletarian, and the capitalist

[1] Theodore W. Schultz, *The Economic Value of Education*, Columbia University Press, New York and London, 1963, p. X.

emphatically a capitalist. The worker's income in the form of wages is the direct opposite of the capitalist's profit: the source of wages is the worker's personal labour, and the source of profit, someone else's unpaid labour. The only difference is that in the past it was the untrained worker doing simple labour who was the main target of exploitation, whereas today it is the working person with a relatively high educational standard and capable of more complex work. Mass unemployment among specialists with a university education, which spread across many capitalist countries in the 1970s, dispelled the illusions about the equal partnership between the "two forms" of capital.

The "human capital" concept took shape at the turn of the 1950*s*, when many Western economists saw education as virtually the most powerful force promoting economic and social progress. Outlays on education came to be seen as investments producing a direct economic effect. A policy on labour power became an integral element in the activity of the capitalist state. As an instrument of state-monopoly regulation, education was now being used to speed up growth, reduce unemployment, moderate the inequality in income, and so on. The "human capital" concept was the ideological mainspring in the effort to work out and substantiate concrete measures.

At the turn of the 1960s, however, the situation changed. The bourgeois education system found itself in a deep financial crisis; there was a down-curve in the economic effectiveness of education; the influx of young boys and girls to college slowed down, and the share of educational investments in the GNP stabilised. These crisis phenomena in the formation of manpower resources in the capitalist countries have undermined the prestige of the "human capital" concept, which has been attacked from different angles. This is a sign of the general crisis of bourgeois economics as a whole.

CHAPTER TWELVE

CONCEPT OF "DEMOCRATISATION OF CAPITAL"

After the Second World War, when the general crisis of capitalism took a turn for the worse, bourgeois economists came up with the concept that capitalist society could be transformed if the working people acquired property.

These views are in effect a version of the old concept of "democratisation of capital", the premises for which arose long ago with the emergence of joint-stock companies, which sought to strengthen their power by mustering the free money resources from every section of the population. Different versions of that concept were advocated in the early 20th century, and the idea of "workers' shares" was recommended at the international Paris congress of businessmen and bankers back in 1889. The crisis of 1929-33 led to a loss of confidence in "workers' shares": these were depreciated and their owners lost the hard-earned savings they had invested in them.

In the past quarter century, the concepts of "people's capitalism" and "democratisation of capital" have been repeatedly brushed up by bourgeois economists in accordance with the structural changes in the economy of state-monopoly capitalism and its strategy in the class struggle. The policy of giving the working people access to property now being followed by a number of capitalist states is yet another experiment in the spirit of "democratisation of capital", the major ingredient of the concept of "people's capitalism".

This policy has been followed most fully and consistently in the Federal Republic of Germany, where the ideas of transforming capitalism through a "fair" redistribution of the national income and the formation of working people's property have become the main weapon in the ideological arsenal of the monopoly bourgeoisie.

1. The "Democratisation of Capital" Concept and the Programmes of the Leading West German Parties

West German economists, speaking on behalf of political parties, businessmen and their unions, have put forward many ideas with respect to the formation of property among the population. All of these boil down to an attempt to substantiate the possibility of "social partnership" between labour and capital, to hinder united action by the working class and its trade unions, and to persuade the working people that their savings guarantee the most realistic way to a classless society.

Various measures are taken to stimulate such savings: premiums and tax benefits in accordance with the West German government's laws on encouraging private housing construction and on premiums on savings; the issue of "people's shares" in view of the privatisation of state-owned enterprises; introduction of new forms of profit-sharing at enterprises; and introduction of so-called investment wages on the basis of wage contracts.

At the same time, to ensure a more even distribution of property among different strata of the population, the left circles of the SPD call for higher taxes on big business.[1]

The slogans and declarations on the formation of working people's property are put forward as an alternative to the nationalisation of private property, which is the goal of sizable sections of the working people.

The "democratisation of capital" concept has become a crucial component of the theory of a "social market economy", which, as it was shown earlier, is pivotal to the economic programme of the CDU, the leading party of the West German monopolies. The idea of people's property and wage workers' participation in productive capital is one of the main provisions in the CDU programme adopted in 1968. Special attention here is devoted to investment wages, which provide for the investment of a share of their increment. The working class has no right to use that share for a number of years.

Bourgeois economists and right-wing trade union leaders (Fritz Burgbacher, Georg Leber, Gottfried Bombach) see investment wages as the most efficient form of compulsory savings and a method of combating inflation. In their opinion, regulation of investment wage rates could become an additional instrument in the policy of economic stabilisation. They believe that the way to curb the "price—wage spiral" is to pay wage workers a share of their wages in a form that would not be consumed but would be retained as property. The main point, they insist, is to save and not to consume the wage increment. The distribution will then allegedly change in favour of the working people, since wage rises do not entail a corresponding increase in consumer

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[1] The most logical way to increase the working people's real share in the national income and the country's wealth would be to raise wages and reduce profits, all the more so since the bourgeois state's income policy enables it to tackle these problems on a national scale, but none of the plans provides for such a perspective.

demand and the employers cannot shift the growing costs onto the consumer. Such is the substance of that concept, which explains inflation by the growth of wages, an explanation directed against the working-class movement.

The social manoeuvring of the bourgeois parties in the Federal Republic of Germany backed by the SPD leaders has also had a definite effect on the West German trade union centre, the Association of West German Trade Unions (AWGTU). Thus, in 1949, the Association's programme emphasised the anti-social nature of the market economy and called for the nationalisation of the key industries, but by the early 1960s the Association had finally abandoned that position. Instead of nationalisation of the key industries, its 1963 programme called for the formation of property among wage workers.

In 1971, the Association's Central Board issued theses on the formation of property, urging all enterprises with a definite rate of income to allocate a share of their profits in the form of securities to decentralised and noncompeting funds which would issue certificates to factory and office workers and government officials with an annual income of no more than DM 24,000 (DM 48,000 for heads of families). The fund should be run by the holders of these certificates and should take due account of state interests.

The theses met with resistance within the Association. Progressive trade union leaders believe that the main way to raise the wage workers' share in the social product is to follow a vigorous wage policy. They reject the formation of property at the expense of wage rises and believe that the social status of wage workers cannot be radically changed as a result of property-forming measures, for the means of production are still in the hands of the capitalists, and this limits the trade unions' possibilities in the struggle to secure higher wages when signing wage agreements. Moreover, the employers use workers' participation in the means of production through employers' funds as an argument against workers' participation in management.

In 1973, the above-mentioned model of property formation was adopted by the Association's federal committee, although the majority was only marginal.

Most West German workers have already signed wage agreements providing for property-forming payments. As a rule, these agreements are initiated and controlled by the entrepreneurs themselves. In these conditions, the trade unions find it much more difficult to secure real wage rises.

The fact that the "democratisation of capital" concept was written into Social-Democratic programmes has had a strong influence on trade union attitudes. This concept was adopted in the SPD's Godesberg Programme, which in effect guarantees protection of private property in the meansof production, for it assumes that socialist transformations can be allegedly achieved through co-participation in management and control over the economic activity of the firms.

Having rejected the Marxist propositions on property, the SPD leadership has finally adopted the postulates of bourgeois political economy. The ideological approximation of Social-Democracy and the bourgeois parties is indicated by the fact that when the SPD leaders came to power they not only continued the CDU/CSU line for a "diffusion" of property, but even came to see it as a goal of their economic policy. Both parties, each in its own way, seek to spread among the masses the ideas of "people's capitalism" through "moderate encouragement" of savings and "diffusion" of property.

The Social-Democratic model of property formation among wage workers provides for their participation in the profits of the entrepreneurs. The question of participation in profits has a long history. Back in 1874, the German Social Policy Union, which brought together German bourgeois economists for the purpose of elaborating measures of "social policy", came out for workers' participation in employers' profits, meeting with the support of the well-known theorist of bourgeois political economy John Stuart Mill, who believed that such participation was not only advantageous for the workers, but also helped to improve society in social terms.

Why is it that questions first formulated more than a century ago have only now been put on the order of the day in the bourgeois state's economic policy?

The answer lies in the conditions of capitalist reproduction, which have changed under the influence of the powerful socialist camp that confronts capitalism and the growing activity of the organised working class in the capitalist countries.

Only today, the capitalist state's economic policy provides (for the first time in practice and not just in theory) for workers' participation in profits. This shows, above all, that the ideological defence of capitalist society now calls for definite material "concessions" on the part of monopoly capital, even to the extent of workers' participation in profits. In reality, however, the idea of broad "diffusion" of property clashes with the goal of capitalist production, which confines its practical implementation to a narrow framework. That is why bourgeois economists, who are obliged to put forward plans for workers' participation in capital, are at the same time doing their utmost to ensure that such participation does not affect the interests of monopoly capital and that these "concessions" do not exceed the minimum that is necessary to justify their social demagogy.

2. "Democratisation of Capital" and State Policy

Up to the mid-1960s, the West German government had carried out a number of measures to "democratise capital", the economic efficiency of which was not even taken into account in determining the main lines of economic policy. The most important measure in the "diffusion" of property was the campaign to privatise state industrial enterprises by issuing "people's shares". Many bourgeois economists, politicians and trade union leaders representing different trends grasped at that idea and advertised "people's shares" as the way to a broad "diffusion" of property in the means of production, to a new stage in the "social market economy", as the way to overcome the antagonisms between labour and capital. The apologetic idea behind that campaign was that with the wide spread of "people's shares" it would be possible to eradicate among the population the ideas of class struggle, of the need to go over to collective property and socialism.

From 1959 to 1965, the state industrial enterprises Preussag, Volkswagen and Veba were partially privatised. The fixed capital of each of these was increased, respectively, from DM 75 million to DM 105 million, from DM 450 million to DM 825 million, and from DM 300 million to DM 600 million. Something like 78, 64 and 60 per cent of the fixed capital was sold in the form of "people's shares". The shares were issued at a value of DM 100, and persons with incomes not exceeding a definite figure had the right to buy these on easy terms at a so-called social rate.[1]

The steps taken to realise the ideological purposes of privatisation did not affect the economic interests

[1] *Ist eine gerechte Einkommensverteilung möglich?*, Herausgegeben von Dr. Klaus Bolz, Wilhelm Goldmann Verlag, Munich, 1972, p. 100.

of monopoly capital. "People's shares" provided state enterprises with additional funds for investment, but did not alter their position in the system of state-monopoly capitalism. To buy "people's shares", the population used cash or savings (in this instance, the purchase amounted only to a change in the form of savings), or reduced their consumption in order to buy these shares on easy terms. But no "democratisation of capital" took place. Nor did the fact that a worker bought two or three shares entail any tangible increase in the family's income through dividends. The only real benefit from the privatisation of state enterprises was that "people's shares" helped them to obtain additional capital by mustering the working people's savings, and were also used for propaganda purposes.

In the 1960s, the emphasis in the formation of working people's property was shifted from privatisation to the policy of encouraging savings, investment wages, and various forms of participation in profits.

The West German state has followed the policy of encouraging savings throughout the whole postwar period. Initially, its main purpose was to buoy the capital market. But when the privatisation campaign was over, without resulting in the "people's capitalism" promised to the working people, the state began to present the efforts to muster their savings as a policy of "democratisation of capital". Use of the savings of broad masses of people for investments is what monopoly capital badly needs under the scientific and technical revolution. Bourgeois economists recommend measures to encourage these savings as the main line in the policy of "diffusing" property. Since the blocking of bank accounts for 5-7 years is the main condition for encouraging savings, there has emerged a new type of property, when the owner's right to use this property is limited. Monopoly capital, on the other hand, is free to use this property in any way it chooses.

The slogan of so-called fair distribution of income and property hinges on an idea shared by many bourgeois economists: that the mass consumer should be turned into a mass investor.

In 1961 and 1965, the government adopted the First and Second laws on encouraging the formation of wage workers' property. These laws provided not only for tax benefits for the working people's voluntary savings, but also for encouragement of payments by entrepreneurs towards the formation of property. These laws were meant to involve the entrepreneurs in the formation of working people's property in order to strengthen the social aspect of the "democratisation of capital" idea, aimed at substituting worker-capitalist "partnership" for the class struggle.

But in its five years, the First Law did not yield any tangible results. Only 380,000 workers resorted to the benefits it offered.

The Second Law markedly widened the range of persons encouraged to save by including officials, lawyers, soldiers and non-working members of their families. Up to its adoption, employers had made payments for the formation of property on the basis of individual contracts and agreements within the framework of the enterprise, but since 1965 encouraged savings have also been determined by wage agreements. In fighting for its vital interests when signing wage agreements, the working class, as represented by the trade unions, confronts an alliance between monopoly capital and the state. The problem of forming working people's property has become a major instrument in the bourgeois state's incomes policy.

Under the Second Law, the share of the income going to form property was at first taxed 8 per cent and later on was exempted from taxes altogether. This was highly advantageous for persons with large incomes, when the tax rate came to 50 per cent, and was of little importance for persons with low incomes. At enterprises with up to 50 employees, the amounts paid to workers for the formation of property could be deduced, within certain limits, from taxable profits.

All these measures, however, had little effect on the distribution of property in the country. Only a highly paid section of the West German population enjoyed the benefits offered by the law. From 1955 to 1969, the share of savings of families with low incomes hardly increased.

The forms of "democratisation of capital" practised up to the 1960s—"co-ownership of enterprises", "workers'", "people's" and "staff" shares, workers' participation in profits—affected an insignificant section of the working people and produced negligible results. The "diffusion" of capital was practised autonomously by a handful of the bigger enterprises and had very little influence on the reproduction of capital.

Some important changes in the ideology of "people's capitalism" and in economic policy took place in the second half of the 1960s, when bourgeois economists unanimously proclaimed the end of the rehabilitation period in the Federal Republic of Germany. Just as they were summing up the results of the "economic miracle", the country was hit by an economic crisis, which showed that the West German economy was subject to the laws of capitalist production with all its contradictions. This was graphically confirmed by the results of a survey of the distribution of property in the country in 1966. That is why, in order to avoid a worsening of social conflicts, the state decided to initiate a broad campaign for the "diffusion of property". Since then, the state has been ever more prominent in property-forming measures, and the policy of forming property among broad sections of the population has come to play the leading role in the state-monopoly regulation of social processes. Property formation is now a separate line of the state's economic policy. The bourgeois state has come to "mediate" between the so-called social partners—monopoly capital and the working class as represented by its trade unions—regulating the formation of working people's property. The methods of exerting an ideological influence on the working class are now being determined in the course of so-called concerted action, involving the Association of West German Trade Unions, whose activity the state seeks to restrict by making it responsible for the results of its own economic policy.

The scale and forms of property-forming policy since the late 1960s have turned this process into an object of state-monopoly regulation, reflecting the ideological, social and economic problems of the reformist idea of integrating the working class into the system of state-monopoly capitalism.

This invites the conclusion that the implementation of the "democratisation of capital" concept has entered a new stage, owing to the following circumstances.

First, to the aggravation of the basic contradiction of capitalism, which manifests itself in the extremely uneven distribution of income and wealth. This unevenness is so deep-rooted and socially dangerous that the state has had to intervene in the distribution of income and wealth and to create at least a semblance of protecting the interests of the poorer sections of the population in order to prevent a social outburst. Second, to the concrete steps to form working people's property on a broader scale, which called for larger outlays not only by employers, but also by the state. And third, to the inclusion of the question of a more even distribution of income and property into the system of goals pursued by the state in its economic policy.

So, the social-reformist concept of "democratisation of capital" has come to be a task of state economic policy, and is being implemented by the state in close alliance with monopoly capital within the framework of an income policy as a set of measures at the stage of income formation.

Social conflicts can no longer be moderated with the help of empty socio-psychological measures or such ineffective measures as the issue of "people's shares". The state's policy for the formation of working people's property reaches such a scale that it affects the whole reproduction mechanism and becomes the object of state-monopoly regulation.

The new stage in the implementation of the socio-reformist concept of "democratisation of capital" has not changed its substance. Private property in the means of production remains intact and the aim is still to protect the interests of monopoly capital. But in view of the changing conditions in which the capitalist system has to exist and its urge to adjust itself to these changes, this old socio-reformist concept has come to play a totally new role under contemporary state-monopoly capitalism. The ideological campaign for the formation of property among the masses is sanctioned by law and is promoted by the state.

At the new stage, practical steps in this area were taken with the adoption of the Third Law on the formation of property, the measures to involve most workers in wage agreements providing for special property-forming payments by the employers, and the drafting and adoption of a government plan for the formation of property among broad sections of the population.

The Third Law, adopted in 1970, envisages a marked increase in property-forming savings as compared with conventional savings. In 1971, 17 million wage workers resorted to the benefits offered by this law (in 1969, the figure was 1 million), and savings that year grew by DM 10,000 million, with premiums and tax benefits amounting to DM 2,000 million. Something like 13.4 million wage workers received payments from their employers for the formation of property. On average, property-forming savings per person in 1971 totalled DM 465.

In January 1974, the Social-Democratic and Free Democratic parties in the Bundestag approved the Basic Provisions of the law on participation in fixed capital, a document regulating the masses' participation in the growth of the fixed capital of enterprises.

Under this plan, the working people do not own capital at a concrete enterprise, but hold shares in funds set up from the profits of major enterprises. So, "social partnership" is raised from the level of individual enterprises to that of the class as a whole. The bourgeois idea of giving the worker a stake in the growth of the enterprise that employs him is supplemented with the idea of giving the whole working class a stake in the growth of the capitalist economy.

The plan, proposed by the government coalition, was sharply criticised by influential trade unions, which justly pointed out that the working class had nothing to gain from this plan. The conversion of factory and office workers into "co-owners" of productive capital does not give them a say in management, and participation in the capital fund to the amount of DM 212 a year merely hinders their struggle for higher wages when signing wage agreements with the employers. Considering the current rate of inflation, the fact that this amount, however small, cannot be used for seven years entails a rapid depreciation of savings. Just as the possession of a few shares does not turn the worker into a capitalist and does not give him a say in decision-making in the corporation, the title to property in the form of investment certificates, bonds or small shares distributed by the funds does not prevent the capitalists from controlling the means of production. Although the implementation of this plan will, perhaps, somewhat increase the working people's savings, in the final count it cannot ensure a fairer distribution of property.

At the same time, the employers' material "sacrifices" envisaged by the plan are not as great as it would appear at first sight, to say nothing of the fact that it is just a matter of restoring to the working class but a small share of what belongs to it by right. In order to prevent the wage worker from "squandering" his property, all the plans provide for long periods during which the "owner" cannot use his savings, whereas the employers can handle these as investments. In the case of investment wages, a share of the wages paid to the personnel of the enterprise is also used for the same purpose.

The monopolies have broad opportunities to compensate for property-forming payments through monopoly prices and the state's taxation policy. True, the favourable terms on which the employer takes part in the property-forming campaign do not rule out a share of the profit going to the working people. But monopoly capital has to incur such expenses in order to obtain maximum profit in the new conditions of the reproduction of capital.

The plans for the formation of working people's property are meant for the long term, and any change in the distribution of property is a drawn-out process. It will take time for practice to confirm the worthlessness of the idea of property "diffusion", as of all earlier reformist ideas, and during this period monopoly capital will be able to use the spread of petty-bourgeois illusions to continue its offensive against the working people's interests.

3. "Democratisation of Capital" and Reality

Ever since the war, one of the main tasks of the state's economic activity in the Federal Republic of Germany has been to encourage capital accumulation in every way. It took many steps in this direction: from the 1949 monetary reform, which deprived broad sections of the population of their savings, to the wage policy which serves the interests of the monopolies.

A wide range of measures of taxation, depreciation, credit and monetary policy entailed an unprecedented concentration of property in the hands of monopoly capital at the expense of the state budget, that is, chiefly at the expense of taxes paid by the working people.

In the course of distribution, the monopolies and the state did their utmost to reduce to a minimum the working people's share in the wealth the latter were creating. Exploitation by employers, taxes on wages, and high prices, all these served to reduce the working people's relative share in the national income and to concentrate wealth in the hands of a few property holders. The history of the West German economic policy is a history of restoring old and building up new large fortunes.

In the postwar period, roughly three-quarters of all private wealth was concentrated in the hands of employers and individuals, and one-quarter, in the hands of wage workers and pensioners. According to Wilhelm Krelle, in 1960, there were 14,000 millionaires in West Germany, and in 1969, almost 20,000.[1]

The activities of the state, whose purpose in accordance with the neoliberal doctrine is to eliminate the social injustice engendered by the market economy, have only served to strengthen the rule of the monopolies. The loud talk about the "economic miracle" was meant to cover up the concentration of the bulk of the country's productive capacities in the hands of a small minority. It was the working people and the mass consumer who paid for the "economic miracle". The liberal West German economist Bruno Gleitze wrote:

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[1] Michael Jungblut, *Die Reichen und die Superreichen in Deutschland*, Hoffmann und Campe, 1971, p. 51.

"There have never been so many millionaires in Germany (in the FRG—*Auth.*) as today, and never before have so many billions been concentrated in the hands of a few."[1]

In financing vast state investments from the budget, which largely consists of taxes on wages, the state already includes the working people's earned incomes into the circulation of social capital. The policy of forming working people's property can be seen as a further deepening of this process, as an urge on the part of monopoly capital to use in production an ever greater part of working people's incomes in order to maximise profits, leaving the owners of the incomes in the position of wage workers who are compelled to sell their labour power. It is largely owing to the policy of compulsory savings that the wage fund is now not only a source of effective demand, but to an ever greater extent a source of investment.

Under state-monopoly capitalism, it takes a very small controlling block of shares to ensure the control of the financial oligarchy over the real means of production, and the wider the shares are diffused, the smaller the shareholding that is necessary to ensure such control. It is common knowledge that monopoly capital gained the upper hand in the economy in the course of a struggle against the smaller owners of the means of production. The illusion is now being created that even workers are being turned by monopoly capital into owners of real capital. In fact, however, the "democratisation of capital" is the most disguised and mystified form of involving the working people's savings in capital accumulation.

The policy of encouraging the formation of working people's property in the Federal Republic of

[1] *Ibid.*, p. 39.

Germany, whatever its methods (tax inducements, "people's shares", participation in capital, investment wages, or other forms of savings allegedly helping to transform present-day capitalist society into "people's capitalism"), primarily serves the interests of monopoly capital, which hopes that this policy will help to resist the anti-imperialist tendencies of the working people.

This policy does not entail any marked changes in the property relations in West Germany. Thus, in 1960, 1.7 per cent of the families owned 70 per cent of the country's productive capital, and by 1966, their share had increased to 73.5 per cent. This shows the growing unevenness in the distribution of property.[1]

The concentration of property in the hands of a minority also leads to an uneven distribution of income. In 1965, 4 per cent of the country's taxpayers with an annual income of more than DM 25,000 received one-quarter of the total income, and 81 per cent of taxpayers with less than DM 12,000 a year received only about one-half of the total income. In the recent period, there has been a noticeable change in the distribution of income in favour of the big property holders, whereas the average wage workers' share in the West German national income has declined.[2] This is the result of the extremely uneven distribution of property in the means of production, whose concentration in the hands of a few owners enables them to appropriate a growing share of the national income.

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[1] *WWI—Mitteilungen*, 1971, No. 8-9, p. 251.

[2] In 1950-1972, the share of wage workers' incomes in the West German national income went up from 58.6 per cent to 69.2 per cent. In that period, however, the number of employers dropped by 37.5 per cent, and the number of wage workers increased by 46 per cent, so that, all other conditions being equal, the latter's share in the national income should have gone up by 31 per cent instead of 18 per cent. Calculated from *Statistisches Jahrbuch für die Bundesrepublik Deutschland*, 1953, p. 111; 1974, pp. 138, 508.

Even bourgeois economists have had to admit that private property in the means of production determines a distribution of income which leads to further concentration of property. The leading West German authorities on matters of property Carl Föhl, Manfred Wagner and Leo Kowalski came to this conclusion:

> "Since low incomes are almost fully used up, while a sizable part of high incomes is set aside, and since high incomes largely consist of profit and interest, i.e. of income on property, most of the newly created national wealth inevitably goes to those who already own property. 'Unto everyone who has shall be given'."[1]

State measures to form working people's property may increase the share of families with a title to ownership of fictitious capital. But there is no doubt that real capital will still be controlled by the big monopolies. One should bear in mind, however, that the law on participation in fixed capital is the bourgeoisie's reformist answer to the working class's demands for radical economic transformations, an answer which is meant to strengthen the "social partnership" between labour and capital.

The German Communist Party, on the one hand, exposes the class content of the reformist concept of forming working people's property, and their participation in capital as a method of integrating the working class into the system of state-monopoly capitalism, as deception of the people, as a concession on matters of secondary importance with a view to preserving the rule of the monopoly bourgeoisie. On the other hand, it regards the bourgeois state's reformist laws not only as a trick of the

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[1] Cited in: *Marxistische Blätter*, Frankfort on the Main, May-June 1970, No. 3, p. 10.

legislators, but also as a gain of the working class, which should be used as a bridgehead for continuing the class struggle in new forms, one of which is the struggle for workers' participation in control over production.[1] The GCP is guided by Lenin's tenet that active struggle on the part of the working class can turn the half-hearted and hypocritical "'reforms' under the existing system into strongpoints for an advancing working-class movement"[2] on the way to socialism.

The Communists propose a realistic way for changing distribution in the working people's interests, which is directed against the monopolies and ensures the necessary resources for economic growth. This is the way of fundamental democratic changes, control over investment, larger state investments, cuts in the export of capital and arms outlays, deduction of 50 per cent of all profits into a common fund, and nationalisation of big concerns, banks and insurance monopolies.

The German Communist Party assumes that the struggle of the working class and all the other progressive forces for a democratic renewal of the state and society, for anti-monopoly democracy opens up the road to socialism.

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[1] See: *World Marxist Review*, No. 8, pp. 23-24.

[2] V. I. Lenin, *Collected Works*, Vol. 15, Progress Publishers, Moscow, 1973, p. 440.

CHAPTER THIRTEEN

RADICAL POLITICAL ECONOMY AND THE "NEW LEFT"

This chapter deals with new trends whose emergence shows the narrowing sphere of the ideological influence of bourgeois economic doctrines.

Readjusting themselves under the influence of crisis processes, the traditional schools still play the decisive role in substantiating the economic policy of state-monopoly capitalism. But the masses' growing awareness of its reactionary nature creates an ideological vacuum, which the traditional bourgeois economic schools cannot fill. This promotes the development of new radical trends in bourgeois economics, which seek to hold the masses captive with the help of reformist ideology.

The crisis of petty-bourgeois economics has a considerable role to play in this process. The illusions that free competition can be revived are pitilessly destroyed by the tide of mergers in the developed capitalist countries, which leads to the emergence of supermonopolies with direct government support, and also by the growing inflation, whose source is the monopoly drive to push up prices. At the same time, new politico-economic concepts emerge in the West with the break-up of class and socio-economic relations caused by the scientific and technical revolution. The number of farmers has been shrinking at an unprecedented rate with the ousted farmers joining the ranks of the urban proletariat. The basis of the petty urban bourgeoisie is also being undermined. The owners of small enterprises in the sphere of trade and the services realise ever more clearly that they have very little chance of "making their way" in the business world.

A sizable section of engineers and technicians, and also persons belonging to the "liberal professions" are also being subjected to monopoly oppression. Under the scientific and technical revolution, many of the once privileged intellectual occupations have become massive. In terms of social status and place in the social division of labour, these people are drawing ever closer to the working class. For most of them, the prospect of proletarisation has become quite tangible.

The old theories of intermediate classes, which had their origins in the ideas of Sismondi and Proudhon, no longer express the interests of petty-bourgeois sections in the developed capitalist countries. These theories, fed by the illusions that under capitalism it is possible to create a favourable setting for small-scale production, call for a revival of the past and do not offer any real alternative to the policy of state-monopoly capitalism, which accelerates the social polarisation of society.

Finding themselves midway between bourgeois and proletarian political economy, and disenchanted with their petty-bourgeois ideals, the ideologists of intermediate strata seek to elaborate theories reflecting the contradictory interests of the new social strata taking shape in the industrialised capitalist countries under the scientific and technical revolution.

1. Theoretical and Ideological Positions of Radical Political Economy

The general platform which unites the various oppositional trends known as radical political economy is that its exponents have abandoned the spent postulates of "economics", of so-called "pure theory", which in effect rules out the analysis of social problems.

Although Keynes gave the state priority over the "economic agent", Keynesianism did not go beyond the theoretical postulates of "economics". Keynes believed that the state had to intervene in the operation of market laws only during an economic crisis, when the country's resources were markedly underemployed. He said that once the state helped to ensure so-called full employment and the cycle entered its upward phase, the economy was again governed by the neoclassical market laws, within whose framework marginalist principles were fully applicable.

Marginalism, which emerged back in the 1870s, and which imputed income to the factors of production (land, capital and labour), was directed not only against Marxism, but also against the theory of Ricardo, who focussed his attention on the distribution of income between classes. He proved that the big landowners were a parasitic estate, for they had no right to receive income deducted from value created solely by labour. The Ricardian tradition—to tie in the problem of income distribution with an analysis of class contradictions—was attacked by the whole of vulgar political economy. It adopted only that part of Ricardo's theory which substantiated the decisive role of capital accumulation in economic development. Those who sought to eradicate the "Ricardian tradition", that is, the analysis of the social problems of income distribution, even dropped the very term "political economy".

The myths spun by marginalism and based on everyday notions engendered by the fetishised relations of sale and purchase, proved to be most tenacious in the Western capitalist countries, but today they are falling to the ground. Hence, the institutionalists' call to go back to political economy as a science whose main content should be socio-economic problems. This has promoted the rapid development of the radical trend in political economy, which has to a certain extent gone beyond the framework envisaged by the bourgeois ideologists of institutionalism.

One notable feature of radical political economy is that it recognises Marx's valuable contribution to economic science and seeks to apply some elements of his analysis. But alongside those who sincerely want to make an in-depth study of Marxist political economy and understand the scientific meaning of the revolutionary theory based on it, there are many radical economists who seek to emasculate the revolutionary content of Marx's teaching on the pretext of "reviewing Marxism".

A direct dependence can be established between the growing anti-capitalist feelings among the students and the strengthening positions of radical political economy in Western universities. This is a reflection not only of the need to respond to the students' growing interest in Marxism, but also of the urge to "channel" this interest so as to prevent the development of their revolutionary consciousness.

It is difficult to pinpoint the theoretical and ideological positions of radical political economy, for it consists of extremely diverse trends. This also makes it difficult for bourgeois ideologists to give an eclectic interpretation of radical political economy, and the tendency in the West now is to include among its advocates all those who reject the conservative positions of "economics" and recognise the imperative need to centre theoretical research on socio-economic problems, on the distribution of national income in particular.

As a rule, such economists of the older generation as Joan Robinson, John K. Galbraith and their younger followers, and also the "new left" are seen as representatives of radical political economy. Such a hazy definition of radical political economy has no serious theoretical basis and leads to confusion with respect to the class and ideological sources of the trends within it.

Economists who criticise imperialism from an ethical angle, denouncing its crimes without taking a clearcut stand in the class struggle, are also ranked among the advocates of radical political economy.[1]

Radical political economy has not only been engendered by the crisis of bourgeois political economy as a whole, but also helps to erode the latter's positions.

Economists known as the "new left" have a special place in this trend. Many of them voice the views of the petty bourgeoisie who are being ousted into the ranks of wage labour, but have still not adopted the proletarian ideology in spite of the fact that in property and social status they have already drawn closer to the working class.

The economists reflecting the ideology of the "new left" do not rank themselves with the reformist

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[1] The following works give an idea of the wide spectrum of views representing radical political economy: R. Edwards, A. McEvan, "A Radical Approach to Economics". In: *The American Economic Review*, May 1970; R. Edwards, M. Reich, T. Webkopi (editors). *The Capitalist System. A Radical Analysis of American Society*, Englewood Cliffs (New Jersy), 1972; K. Hunt, H. Sherman, *Economics: An Introduction to Traditional and Radical Views*, New York, 1972; D. Gordon (ed.), *Problems in Political Economy: An Urban Perspective*, Boston, 1970; J. Weaver (ed.), *Modern Political Economy. Radical and Orthodox Views on Crucial Issues*, Boston, 1973.

wing of bourgeois and petty-bourgeois political economy, but, on the contrary, say that they are prepared to attack[1] capitalism and raze it to the ground. Some of them want to be more "left" than the Marxists and formulate socio-economic concepts laying claim to a "new" interpretation of the revolutionary process differing from that of "traditional Marxism". They sharply criticise and expose the vices of the US "consumer society" but, as a rule, have no positive economic programme to offer. Some of the "new left" advocate a blend between Marxism and the anarchist ideas of Proudhon and Kropotkin, or call for a "counter-culture", meaning a "parallel" world within present-day US society, with special settlements, communes, schools, theatres, magazines and even universities.

But although the academic bourgeois circles are shocked at the revolutionary slogans of the "new left", they nevertheless view with indulgence some of the seamingly super-radical trends, primarily those which deny the historical importance of proletarian dictatorship and the socialist nature of the Soviet state. Bourgeois ideologists even see the theories propounded by some of the "new left" as an obstacle to the development of scientific Marxist thought. With this aim in view, they encourage all sorts of petty-bourgeois and anarchist concepts seeking to prove that in the world today it is impossible to orient oneself upon a revolutionary doctrine based on the Marxist-Leninist theory. To justify their eclecticism and utilitarian pragmatism, they resort to false historical analogies that can delude politically naïve and inexperienced men and women. Thus, the advocates of pluralism in ideological trends and theoretical concepts, who are against the unity of the revolutionary forces, refer, for instance, to the activity of the First International, which, they say, was equally determined by the Marxists and by the followers of Proudhon and Bakunin. They belittle

Marx's role as the founder of the First International and ignore his struggle against the followers of Proudhon and Bakunin. They also depreciate the role played by Lenin and the Bolshevik Party in the Great October Revolution. Falsifying history, they insist that representatives of different trends—Social-Democrats, Socialist-Revolutionaries and anarchists, equipped, respectively, with the theories of Marx, Proudhon, Bakunin and Kropotkin—equally contributed to the revolution in Russia.

The facts refute the pseudo-scientific theories of eclectic "pluralism", which ignore the real historical laws of the class struggle.

The Socialists of the pre-Marxian era, the Proudhonists and Bakuninists, who took part in the First International and the Paris Commune, had petty-bourgeois social origins and reflected petty-bourgeois attitudes. It was only natural that they advocated subjective-psychological idealistic views, voluntarism and adventurist tactics. They could not understand scientific socialism, the theoretical expression of working-class interests. Lenin said that in the theoretical plane anarchism had "produced nothing but general platitudes against *exploitation*".[1] The SRs and anarchists in Russia were opponents of Marxism, and this eventually put their leaders in the counter-revolutionary camp.

The advocates of present-day "pre-Marxian socialism" have come out not only against the theory of scientific socialism, but also against socialism itself, which has become a historical reality owing to the victories of the working class led by its vanguard, the Marxist-Leninist parties, equipped with this theory.

Other economists ranking themselves with the "new left" take an anti-historical, metaphysical

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[1] V. I. Lenin, *Collected Works*, Vol. 5, Progress Publishers, Moscow, 1972, p. 327.

view of reality. They ignore the fundamental propositions of historical materialism on the succession of socio-economic formations and the laws of the class struggle. They see the material basis of revolution in the introduction of a crude egalitarian system of distribution rather than in a transition to a higher stage of production, which creates opportunities for the allround development of the individual and for true social equality.

Marx believed that petty-bourgeois egalitarian communism was an expression of private-property notions, which were at odds with the goal of building up a society that would inherit and multiply all the achievements of civilisation in the interests of the working people.

> "The thought of every piece of private property as such is *at least* turned against *wealthier* private property in the form of envy and the urge to reduce things to a common level, so that this envy and urge even constitute the essence of competition. Crude communism is only the culmination of this envy and of this levelling-down proceeding from the *preconceived* minimum. It has a *definite*, *limited* standard."[1]

Although in the pre-Marxian period crude egalitarian communism played a progressive role in criticising capitalism and promoting the revolutionary struggle, Marx and Engels did not make any allowances for it, denouncing its erroneus politico-economic concepts. They wrote in the *Manifesto of the Communist Party*:

> "The revolutionary literature that accompanied these first movements of the proleta-

[1] Karl Marx and Frederick Engels, *Collected Works*, Vol. 3, p. 295.

riat had necessarily a reactionary character. It inculcated universal asceticism and social levelling in its crudest form."[1]

2. Contradictory Tendencies in the Political Economy of the "New Left"

Today, the tendencies of crude egalitarian communism are fed by the social sections that easily submit to the primitive notions of petty-bourgeois egalitarianism, which starts from the assumption that economic equality can allegedly be achieved through purely political measures.

In the developed capitalist countries, egalitarian petty-bourgeois theories most easily affect uprooted semi-proletarians, lumpen elements, and the middle strata of town and country, who hate the rich and the powers that be. They fall for the illusion that the existing state of affairs can be rapidly changed without any fundamental transformations in the whole system of the mode of production and social relations.

Reflecting these attitudes, some of the "new left" believe that revolutionary strategy should be based not only on a struggle between the bourgeoisie and the working class, but on a clash between the "rich" and the "poor" on the international arena, as well as within individual countries. In spite of their apparently anti-capitalist tenor, such concepts are often used by bourgeois economics to realise its class purposes. Thus, the idea being spread by some of the "new left" that the working class in the richer capitalist countries has "degenerated" and "gone bourgeois" help bourgeois economists to attack the trade unions, to blame the inflation on their "excessive demands", and to secure bans on strikes in the name of "law and order". Bourgeois

[1] *Ibid.*, Vol. 6, p. 514.

theorists have also quite successfully made use of the contrast between the "new working class", which is said to include "white collar workers" (employees and the intelligentsia), and its other contingents. Such concepts theoretically justify the sectarian contempt towards the struggle for working-class unity, indispensable for a victory over capitalism.

But although radical political economy seeks to integrate the economic theories of the "new left", these do not form a single social stream. An ever greater role here belongs to the advocates of genuine anti-imperialist action, whose aim is not only to master the Marxist-Leninist theory, but to apply it in practice. In radical political economy, which is far from homogeneous in class terms, one should primarily distinguish between the bourgeois and the petty-bourgeois wing.

In contrast to bourgeois apologists, who champion big private capitalist property in the means of production, petty-bourgeois theorists attack it and call for its "fair" redistribution. The petty-bourgeois inclination to waver between the bourgeoisie and the proletariat and try to steer a "middle course" can be used both in the interests of the bourgeoisie and in the interests of the working class. Hence the need to win over the petty-bourgeois strata of the working people to the side of the working class, patiently to explain their theoretical delusions, and to direct principled and convincing criticism at their sociological concepts, which are permeated with an anti-imperialist spirit, but at the same time can divert them from the high road leading to a victory over imperialism.

So, the analysis of the class roots and social orientation of the various trends within radical political economy shows that these cannot be reduced to a single denominator. One should distinguish its bourgeois wing, which, while criticising traditional vulgar political economy, still clings to its methodological positions, from oppositional petty-bourgeois trends.

In the past few years, radical political economy has secured recognition of its "sovereign rights" in the universities and on the book market, for bourgeois ideologists realise that radical political economy is not the chief adversary of the traditional trends of bourgeois political economy; they have to reckon with the fact that the major opponent of bourgeois economic concepts—both old and new—is Marxist-Leninist political economy, which is being developed and enriched on the basis of a theoretical generalisation of the experience of world socialism, the working-class and national liberation movements — the interrelated forces of the world revolutionary process.

Now that the masses in the developed capitalist countries have become more politically conscious, so that the "communist bogey" can no longer be used as a serious weapon in the arsenal of ideological struggle, bourgeois ideologists have had to change the very methods of this struggle. Thus, it is being said that "traditional Marxism" is "dogmatic" and "obsolete", and takes no account of the latest economic and social phenomena.

But under the present competition between the two systems—the major form of the class struggle on the international scene—these methods of theoretical and ideological struggle are also doomed to failure. The course of historical events proves ever more convincingly that, far from being obsolete, the Marxist theory is permeated with the spirit of innovation.

The attempts to present "traditional Marxism" as an ossified dogma cannot be successful, like the attempts to contrast the Marxist-Leninist economic theory with various versions of "legal Marxism" or "innovatory" anti-Marxist writings, engendered by the narrow-mindedness of petty-bourgeois elements in their search for a "middle" road.

3. The Growing Influence of Marxist-Leninist Political Economy

Marxist-Leninist political economy has developed with the use of all the achievements of modern science. It has enriched the methods of its research on the basis of discoveries in natural science, which enable it extensively to apply the methods of quantitative analysis, and also the achievements of psychology and sociology in order to take into account more fully and comprehensively man's possibilities and requirements, for man's wellbeing and allround development is the major goal of socialism.

In the more than a century since the emergence of Marxism, there have been many attempts to formulate an economic theory that could hold its ground against Marxism. In many instances, the adversaries of Marxism have come out as "innovators", seeking to substantiate their theories with the latest scientific discoveries and new social phenomena. But history has invariably disproved the theories of these false prophets.

Here is what Lenin, who truly developed Marx's economic theory in a creative spirit with a view to the achievements of world science and new social phenomena, said in this context:

> "I still stick to my old ideas that after Marx you can drag in non-Marxian political economy only for the purpose of fooling philistines, even if they are 'highly civilised' philistines."[1]

Radical political economy, among whose advocates there are many self-styled "prophets", is least of all able to challenge the Marxist-Leninist economic theory. Its very name, "radical political economy", is largely artificial, for it in effect does not

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[1] V. I. Lenin, *Collected Works*, Vol. 33, Progress Publishers, Moscow, 1966, p. 408.

exist as an integral economic theory. It is a conglomerate of different trends engendered by the crisis and disintegration of bourgeois political economy.

But one cannot ignore the fact that radical political economy, however amorphous and indefinite, reflects the ideology and interests of the intermediate social strata in the industrialised capitalist countries today. While essentially remaining a petty-bourgeois political economy, it differs from the old schools. In contrast to the traditional petty-bourgeois critics of the monopolies, who advocate a return to free competition, radical economists, especially those belonging to the "new left", have resolutely denied the positive role of capitalist competition. Most radical economists realise that capitalism should give way to a new society, but cannot formulate a realistic programme for the advent of such a society.

As I pointed out earlier, radical economists take a middle stand between bourgeois and proletarian political economy. In our historical epoch, however, the logic of the class struggle makes the choice inevitable. In these conditions a process of differentiation is bound to occur. Some of the radical economists sincerely fighting against imperialist crimes (as "socialists at heart") are bound to go over to the side of the working class, whose interests are most consistently expressed by Marxist-Leninist political economy.

It starts from the fundamental theoretical conclusion that, owing to the objective laws of the development of the productive forces and the resulting changes in the relations of production, capitalism turns most men and women into wage labourers, and production itself into social production, so laying the ground for its revolutionary transformation. The strategy and tactics of the working class's revolutionary struggle consist in winning the support of an overwhelming majority of the people, who can overpower the small minority of reactionaries seeking to hold back historical development.

Marxist-Leninists, who are convinced of the superiority of their scientific theory and the attractiveness of humane communist ideas, and who rely on the objective laws of economic development and the class struggle, are working for a broad popular anti-imperialist coalition both in individual capitalist countries and on an international scale. With this aim in view, they are prepared to hold theoretical disputes with the participants in such a coalition, taking an irreconcilable stand for their abiding ideological principles.

CHAPTER FOURTEEN

THE GENERAL CRISIS OF CAPITALISM AND BOURGEOIS ECONOMIC DOCTRINES OF WORLD DEVELOPMENT

The bankruptcy of the bourgeois politico-economic doctrines considered in earlier chapters is due not only to the aggravation of capitalist society's contradictions, but also to the influence exerted on the world capitalist system by outside forces, namely, by the uniformities of the growth and strengthening of world socialism, which are becoming the crucial factors of world history. They engender the global confrontation between the two systems, which primarily manifests itself in the economic competition between them, and create a favourable setting for the national liberation movement, which erodes the imperialist structure of the world economy. The growth of socialism and its spread to a number of countries inevitably explodes the bourgeois economic doctrines of world development which constitute a major section of vulgar apologetic political economy. Nor can these doctrines serve any longer as a theoretical substantiation of imperialist strategy in international relations.

Every theory is tested in practice. The crisis of bourgeois economics is primarily due to the bankruptcy of the economic policy based on its doctrines. This crisis makes it necessary to develop new doctrines of economic policy, which capitalist apologists formulate on the strength of the postulates of bourgeois economics aimed at ensuring the rule of capital over labour. There can be no other economic policy in countries where the rule of capital is still intact. That is why the bankruptcy of this or that doctrine of economic policy cannot be identified with a collapse of all the postulates of bourgeois economics as a theory expressing the class interests of the capitalists. There is a well-known Marxist proposition that the ideas of the exploitive ruling class predominate in society so long as that class has political power, which enables it to hold in spiritual bondage a sizable section of the working people.

But in one area of the ideological contest between the bourgeoisie and the working class—the bourgeois theories of world economic development—it is not only the economic doctrines, but also the theoretical postulates of bourgeois economics that have gone bankrupt. These theories are refuted by the practice of the world revolutionary process and the deepening general crisis of capitalism.

Marxist-Leninist parties in all countries of the world devote vast attention to studying the uniformities of the general crisis of capitalism.

This is so because, first, the objective economic uniformities of the general crisis of capitalism determine the strategy of the revolutionary struggle, its long-term tendencies on a global scale. A correct strategy is decisive for the choice of forms and means of struggle. The uniformities of economic and political development are not straightforward. In analysing the economic laws of capitalism, Marx noted that these uniformities manifest themselves as tendencies of development. The predominant tendency reflecting a uniformity is offset by countertendencies, but the predominant tendency is invincible. In this sense, history is "tendentious": it always sides with socially progressive classes and condemns to death the classes that seek to reverse the tide of history and pull mankind back to past historical stages. Scientific cognition of the objective laws of development and their correct interpretation are crucial to the victory of the ascendant class.

Second, the exceptional attention attached by Marxist thinkers to the theory of the general crisis of capitalism is due to the fact that this theory is an arena of intensive ideological struggle. Western theorists ignore the deep-going uniformities of world history relating to the succession of socio-economic formations. Instead of bringing out these uniformities, they analyse the short-term situation and take a superficial view of reality. Western economists think it possible to correct capitalist society's "shortcomings", which are allegedly due to upsets in the functional ties within its economic system, to improve it through reform, and refute the Marxist-Leninist conclusion on the inevitable collapse of the last exploitive system, whose historical purpose is to prepare the material and social prerequisites for mankind's transition to communism.

In their ideological struggle against bourgeois economics, Marxist thinkers rely on the fundamental analysis of the uniformities of capitalist society's disintegration established by Marx, Engels and Lenin, and also on the theoretical generalisation of the concrete historical development of present-day capitalism contained in the documents of the CPSU and other Communist parties.

A comparison of the forecasts made by bourgeois economists with historical reality over the long term and on a global scale inevitably shows the triumph of Marxist-Leninist political economy in the struggle against bourgeois concepts.

1. The Theory of the General Crisis of Capitalism and the Basic Postulates of Bourgeois Political Economy

Marx based his conclusion that revolutions and the downfall of the capitalist formation were inevitable on two fundamental uniformities he discovered.

The first is that the relations of production always correspond to the nature of the productive forces. Marx proved that at a definite stage of growth capitalist productive forces come into contradiction with the relations of production, which no longer promote the development of the productive forces but fetter these, ushering in the epoch of social revolution.

The second fundamental uniformity is that machine production, which embodies the productive forces corresponding to capitalism, engenders the proletarian class, which comes to stand at the head of mankind's struggle for a better future.

Marx made these theoretical generalisations on the strength of an analysis of concrete historical development. The economic crises of 1825 and 1847 showed that capitalism could not give free scope for the development of the productive forces. The uprising of the Lyon weavers in 1830 and the Chartist movement in England in 1830-40 showed the working class's will and ability to wage a political struggle against the bourgeoisie.

Marx analysed the interplay of the productive forces and the relations of production on a global scale. It was capitalism itself that paved the way for regarding the world as a single whole by creating the world market. Marx saw the development of the world market as the chief mission of bourgeois society. The capitalist epoch gave rise to the international division of labour, which marked a gigantic stride forward in the development of the productive forces. Marx wrote:

> "Thanks to the application of machinery and of steam, the division of labour was able to assume such dimensions that large-scale industry, detached from the national soil, depends entirely on the world market, on international exchange, on an international division of labour."[1]

But capitalism cannot develop the international division of labour on the basis of peaceful relations among nations enjoying its advantages. This is capitalism's Achilles heel, one of the main reasons behind its decline and the start of the world socialist revolution, born from a global aggravation of contradictions between the productive forces and the relations of production.

The First World War brought out these contradictions to their full extent. During the war, Lenin used Marx's method to show the inevitability of the impending socialist revolution and the general crisis of capitalism. He wrote:

> "Marx's method consists, first of all, in taking due account of the *objective* content of a historical process at a given moment, in definite and concrete conditions; this is in order to realise, in the first place, the movement of *which* class is the mainspring of the progress possible in those concrete conditions."[2]

At a time when apologetic bourgeois political economy glorified the progressive mission of capitalism in the development of the productive forces, Lenin established that deep-going social upheavals were gathering head in the entrails of capitalism.

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[1] Karl Marx, Frederick Engels, *Collected Works*, Vol. 6, p. 187.

[2] V. I. Lenin, *Collected Works*, Vol. 21, p. 143.

In an article entitled "Under a False Flag", written in 1915, Lenin proved this beyond any doubt on the strength of an analysis of the tendencies of global historical development, and his proof is still relevant today. He pointed out that the bourgeoisie had played a historically progressive role in the development of the productive forces only in the first epoch of modern history, which had started with the French bourgeois revolution in 1789 and ended in 1871. It had been

> "an epoch of bourgeois-democratic movements in general and of bourgeois-national movements in particular, an epoch of the rapid breakdown of the obsolete feudal-absolutist institutions."[1]

Then came the second epoch of modern history, that

> "of the full domination and decline of the bourgeoisie, one of transition from its progressive character towards reactionary and even ultra-reactionary finance capital ... an epoch in which a new class—present-day democracy—is preparing and slowly mustering its forces."[2]

In that period, it is no longer the export of commodities, but the export of capital that becomes the decisive form of economic ties and is connected with a tendency towards monopoly domination of the market and monopoly rule of territories through annexation.

That period of modern history ended with the outbreak of the imperialist world war, which started the third epoch and was the result of the use of the most reactionary methods of struggle for an expansion of the markets with the help of "local wars" for monopoly ownership of territory. The

[1] *Ibid.*, p. 146.
[2] *Ibid.*

struggle for a redivision and subjugation of colonial empires, ruled by nationally isolated groups of the financial oligarchy, became a "legalised" instrument in the expanded reproduction of capital. In this way, monopoly capital sought to ensure the development of its production base, which outgrew the framework of national states. Militarisation of the economy and the arms race were among the inevitable costs in the deformative development of capitalist productive forces and the international division of labour at its imperialist stage.

Lenin wrote:

> "The bourgeois-national state framework, which in the first epoch was the mainstay of the *development* of the productive forces of a humanity that was liberating itself from feudalism, has now, in the third epoch, become a *hindrance* to the further development of the productive forces. From a rising and progressive class the bourgeoisie has turned into a declining, decadent, and reactionary class. It is quite another class that is now on the upgrade on a broad historical scale."[1]

This "decadent" class played its extremely reactionary role not only by fattening on the production of lethal weapons and plunder of the colonies. Once the bourgeoisie had destroyed the main bastions of feudalism in Europe, it took up a policy of conserving and implanting slave-holding and feudal forms of exploitation in the colonies it had seized. Emphasising this cardinal fact, which shows the reactionary nature of the monopoly bourgeoisie, and pointing out that the world war was a war to redivide the colonies, Lenin noted:

> "The third epoch, which has just set in, places the bourgeoisie in the same 'position'

[1] *Ibid.*, p. 149.

as that in which the feudal lords found themselves during the first epoch."[1]

In these conditions, when the bourgeoisie of the imperialist countries had become utterly reactionary, the working class—the only revolutionary class—was called upon by history to ensure the development of the productive forces on the scale of the world economy. First of all, it was necessary to destroy the imperialist structure of the world economy. At the same time, the working class had to put an end to world wars, which had made the domination of monopoly capital with its imperialist policy the most sanguinary epoch in mankind's history.

In June 1918, when German imperialism hoped to strengthen its war machine by occupying Soviet territory taken over on the basis of the fettering Brest Peace, and the Entente was prepared to continue the war to a victorious end with the help of the growing US military-economic potential recently involved in the war, Lenin characterised the untold suffering inflicted by the war and the imperialists' reckless urge to continue the massacre, and came to an extremely important theoretical conclusion on the nature of the crisis of capitalism engendered by the global scale of the imperialist world war. As he pointed out, the war would inevitably "undermine the very foundations of human society",[2] and emphasised that the task now was "the preservation of human society".[3]

The historically imperative need to eliminate imperialist wars from the life of society and lay the groundwork for peace and friendship among nations was marked by the victory of the Great October Socialist Revolution, which enabled Eura-

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[1] *Ibid.*, p. 146.

[2] V. I. Lenin, *Collected Works*, Vol. 27, Progress Publishers, Moscow, 1977, p. 422.

[3] *Ibid.*, p. 425,

sia's biggest state to withdraw from the war, made a gigantic breach in the world capitalist economy, paved the way for building the world's first socialist state and a qualitatively new world economy based on coexistence and economic competition between the two antagonistic social systems.

2. The Bankruptcy of Imperialist Apologetics

Criticism of bourgeois and reformist concepts of world economic development was a major element in Lenin's theoretical activity in preparing the October Revolution.

Lenin continued the research started by Marx in his *Capital* and analysed the qualitative changes in the development of the contradictions between the productive forces and the relations of production, caused by the capitalist methods of socialisation of production under monopoly rule.

On the strength of that analysis, he predicted that imperialist world wars were inevitable, that capitalism would develop unevenly, that a socialist revolution could not win out simultaneously in all the capitalist countries, and that the world revolutionary process would unfold against the background of an economic competition and peaceful coexistence between capitalism and socialism, in the course of which world economic ties would take shape on the basis of international division of labour involving the two contending modes of production.

To counter the theory of progressing international division of labour as the chief factor in the development of the productive forces in the interests of the whole of mankind, which Marxism had raised to a new stage, the ideologists of the monopoly bourgeoisie not only formulated apologetic concepts of vulgar political economy, but also sought to spread great-power nationalism and imperialism.

In their evolution, the bourgeois theories of international division of labour took various forms, which expressed the interests of the bourgeoisie of both dominant and small nations. Thus, the theory of free trade, which stemmed from Smith and Ricardo's doctrine of the international division of labour, was used by England back in the mid-19th century, when capitalism was still on the whole progressive, to consolidate its monopoly as the "world's industrial workshop". In contrast to that theory, the German economist Friedrich List formulated the concept of a national economy, which raised tariff barriers against foreign competition. His concept reflected the striving of young capitalist states to take a stand against the monopoly of English industry, in order to build up an industrial basis for their own economy. But List's theory was subsequently used to justify the aggressive imperialist protectionism of these young states and the ideas of economic autarky, serving to vindicate their policy of militarising the economy. So, the bourgeois concepts of the world economy were purged of all progressive ideas and helped monopoly capital to manipulate the masses for its own imperialist purposes.

In the imperialist epoch, the gnosiological horizon of bourgeois political economy markedly narrowed down. Its traditional theories of the international division of labour were based on the exchange concept. That was more or less natural in an epoch when the world market was taking shape and when the exchange of commodities was the main form of economic ties between states. At the turn of the 19th century, when the world capitalist market was beginning to take form and the export of commodities was giving way to the export of capital as the crucial form of economic ties, vulgar bourgeois political economy was even less able to understand the substance of the international division of labour. The exchange concept could not explain, even superficially, the formation of the world capitalist economy. Still, it became even more important as an instrument of apologetics, aimed to conceal the ever more reactionary essence of the international capitalist division of labour.

That was why Lenin subjected to withering criticism bourgeois theories of the world economy based on the exchange concept. In his *Notebooks on Imperialism* Lenin considers from this angle the methodological principles in the works of Sigmund Schilder, Richard Calwer, Bernhard Harms, Eugene Agahd and others. Here is what he wrote about Schilder's book, *Development Trends in the World Economy*, Vol. I, Berlin, 1912. (Vol. I: *Planned?! Influence on the World Economy*):

> "The title is too sweeping, the subtitle plainly fraudulent, for the author has specialised in tariff policy=there you have his planned influence!!"[1]

What made the title too sweeping was that the book dealt with world trade, whereas the tendencies of world economic development, as Lenin had convincingly shown in his analysis of imperialism, were determined by the export of capital, which had led to the domination of the imperialist states' financial oligarchy over a vast majority of mankind. In contrast to the exchange of commodities, the export of capital gave rise to long-term and constantly reproduced relations of dependence between the creditor and the debtor countries. Ever more states were turning into interconnected links of the world economy. The export of capital entrenched the imperialist states' monopoly right to exploit any unoccupied territory rich in raw material deposits, proved or potential. The imperialist tendency now was to form closed colonial empires enabling the metropolitan country to invest capital on the most favourable terms, and also to form

[1] V. I. Lenin, *Collected Works*, Vol. 39, Progress Publishers, Moscow, 1968, p. 96.

monopoly markets guaranteeing them from the vicissitudes of competition. The export of capital enhanced the role of coercive, non-economic methods in the exploitation of the colonies. The advent of the imperialist epoch was marked by "local wars" for a seizure and redivision of colonies.

From the standpoint of the financial oligarchy, these wars were not even considered to be real wars. In Europe, there had been no wars for more than 40 years, ever since Prussia had defeated the French army at Sedan, and the two adversaries had joined forces to suppress the Paris Commune in 1871. The population of the metropolitan countries had the illusion that their territory was free of wars once and for all. This enabled bourgeois apologists to extoll the new forms of monopoly expansion based on the export of capital and its international interlacing, and to paint idyllic pictures of world economic development and harmonious international division of labour. The revisionist Karl Kautsky echoed these views. He tried to prove that the growing international interlacing of capitals would lead to the establishment of a global trust and moderate imperialist contradictions. Exposing his conclusions, Lenin wrote:

> "Kautsky's utterly meaningless talk about ultraimperialism encourages, among other things, that profoundly mistaken idea which only brings grist to the mill of the apologists of imperialism, i.e., that the rule of finance capital *lessens* the unevenness and contradictions inherent in the world economy, whereas in reality it *increases* them."[1]

When the world war broke out, bourgeois and social-imperialist theorists could not explain its causes.

These theorists, who ignored the decisive role of the export of capital in the international division

[1] V. I. Lenin, *Collected Works*, Vol. 22, p. 272.

of labour, also "overlooked" another major feature of the imperialist epoch. The export of capital to the colonies and semi-colonies promoted the emergence in the latter of two new classes, the industrial proletariat and the national bourgeoisie, which were to play a crucial role in the national liberation movement that subsequently led to the collapse of the colonial system of imperialism.

During the First World War and the early postwar years, Lenin made a comprehensive theoretical analysis of the way in which capitalism had exhausted its progressive mission in the international division of labour and showed that the imperialist concepts of the world economy were quite worthless.

He showed that capitalism, which had made imperialist wars an instrument of competition, had exhausted its progressive historical role in the development of the productive forces. With capitalist society's transition to its state-monopoly stage, militarism—the production of destructive forces—becomes its integral feature not only in time of war, but also in peacetime. Lenin proved that these conditions necessitated a world socialist revolution, which was to create conditions for the development of the productive forces on the basis of a fundamentally new international division of labour in the interests of the whole of mankind.

From the methodological standpoint, one important point to recall in arguing against our ideological opponents—bourgeois economists—is that the general crisis of capitalism was triggered off by the First World War. It was that war, and not the socialist revolution or civil wars, that threw the world economy into chaos. The war clearly showed that the bourgeoisie could not ensure the development of the productive forces on the scale of the world capitalist economy.

The socialist revolution had the creative potential to overcome the chaos and anarchy in the international division of labour. This tendency, noted by Lenin, has distinctly manifested itself at every stage of the general crisis of capitalism. One irresistible uniformity of social development, which makes it imperative to prevent world wars so as to ensure the progressive development of the global productive forces, is that at every new stage of the general crisis of capitalism the sphere of imperialist domination is narrowed down under the onslaught of the revolutionary forces. The laws of history work for peace.

L. I. Breshnev said at the World Congress of Peace Forces:

> "Our philosophy of peace is a philosophy of historical optimism. Though the present situation is complicated and contradictory, we are confident that the broad peace offensive now under way will be successful."[1]

The world revolutionary process which unfolded after the October Revolution and whose main content is the worldwide transition from capitalism to socialism, has entailed the collapse of all the colonial empires and raised an insurmountable barrier in the way of the financial oligarchy's efforts to build up new empires, including those disguised by a neocolonialist screen.[2]

The victory over fascism in the Second World War, in which the decisive role was played by the Soviet Union, fighting together with the capitalist countries of the anti-fascist coalition, the Resistance movement on the territories occupied by the aggressors, and the national liberation movement of the colonial peoples, who saw fascism as a force seeking to perpetuate colonialism, showed that the

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[1] L. I. Brezhnev, *Following Lenin's Course*, Speeches and Articles, Progress Publishers, Moscow, 1975, p. 327.

[2] The last of the colonial empires was eliminated by the anti-fascist revolution in Portugal in April 1974, which joined forces with the national liberation movement in Portugal's overseas territories.

attempts to bring back the epoch of the formation of world empires were doomed to failure.

After the Second World War, bourgeois economists set out to prove that it was necessary and possible to maintain the historically conditioned economic ties between the metropolitan countries and the young national states on the basis of "partnership" which, they believed, would guarantee profitable investments for private capital. Another element of neocolonialist policy was military aid to reactionary regimes set up by the social sections in the developing countries which hope to prolong their existence as accomplices of imperialism.

But under the steadily developing world revolutionary process, monopoly capital, even with the help of neocolonialism, cannot retain the privileges it has inherited from the epoch of imperialist enslavement.

There were two historic events marking the beginning of the crisis of neocolonialist policy and the postwar imperialist structure of the world capitalist economy.

First, the 15-year-long US intervention in Indochina came to an end in 1975 with the military defeat of US imperialism and the collapse of the Saigon puppet regime. That showed the crisis not only of neocolonialism, but also of the cold war strategy directed against the socialist countries.

The second serious factor in the crisis of the neocolonialist system was that imperialism lost its raw material monopoly in many developing countries. This process rapidly intensified starting in October 1973, when in protest against the US support of Israeli aggression the Arab countries put an embargo on oil exports to the United States and quadrupled the price of exported oil. Simultaneously, a number of Arab countries nationalised the oil fields owned by imperialist multinational corporations. This started a chain reaction of price rises in oil and other fuels and raw materials, and other developing countries took steps to nationalise the property of multinational corporations.

Such nationalisation markedly strengthened the positions of the public sector in many developing countries. High prices of exported raw materials enabled some of them to accumulate sizable financial resources, giving them an opportunity to industrialise their economy and free themselves from the historically conditioned economic dependence on the imperialist powers. At the same time, the sharp growth of the state budget made it possible to carry out social measures to develop education, improve the health service and raise the people's cultural standards.

The US military defeat in Indochina in 1975 made it clear that the imperialists could not restore their monopoly on raw material sources through armed intervention simultaneously directed against many developing countries, which resolutely exercised by means of nationalisation their sovereign right to use their own raw material resources.

The disintegration of the imperialist structure of the world capitalist economy under the influence of the revolutionary process (whose power is due to the growing strength of the socialist community, the intensifying struggle of the working class against monopoly rule, and the unprecedented scale of the national liberation movement for a total eradication of the colonialist aftermath) goes hand in hand with the collapse of the last bastions of slavery and feudalism in capitalism's colonial periphery, which hinder the development of the global productive forces. In most developing countries, large feudal estates are being eliminated either through revolutions from below or through reform from above, the land is handed over to those who work it, and class privileges are being abolished. The light of science and knowledge is dispelling the gloom of the Middle Ages.

The motive forces behind this world historic development, based on the class struggle between socialism and capitalism (the contest between the two modes of production and the corresponding ideological confrontation), are best brought out by an analysis of the strategic tasks being carried out by the revolutionary forces at each stage of the general crisis of capitalism.

This also helps to bring out the most important features characterising the bankruptcy of bourgeois theories of the international division of labour, and of related doctrines spearheaded against the revolutionary forces.

Even in those periods of history when imperialism was economically and militarily stronger than socialism, the Marxists took an optimistic view of history, orienting their policy with a view to the fundamental uniformities of social development. Their optimism is based, among other things, on the undeniable fact that the October Revolution was not a historical accident, but reflected the objective requirements of social development, starting the irreversible process of the revolutionary transformation of the productive forces and relations of production on a global scale.

The forecasts of bourgeois politicians and economists, who argued that the Soviet state was nonviable and the socialist revolution had no prospects ahead of it, forecasts which served as guidelines for imperialist strategy, were refuted by history at the very first stage of the general crisis of capitalism. Back in the early 1920s, the imperialist countries had to stop their policy of armed intervention and economic blockade against Soviet Russia. They had to do this in view of the "Hands Off Soviet Russia" working-class movement in their own countries and the economic crisis of 1920-21, which made the capitalists look for opportunities of expanding their markets through trade with the world's first socialist state.

But bourgeois economists still hoped that the "socialist experiment" would fail. Soviet Russia's new economic policy, aimed at strengthening the positions of socialism, was interpreted as a victory of the market economy over the planning principles of the Soviet economy, with an inevitable restoration of capitalism. At that time, it was the neoclassics who set the fashion in bourgeois economic science. They maintained that a state-controlled planned economy could not function, for it contradicted the laws of the market, which they saw as the only mechanism capable of taking into account society's real requirements. Socialism was contrasted with the US economy, where the operation of spontaneous market forces allegedly provided the key to "everlasting prosperity".

But the disastrous economic crisis of 1929-33 dispelled the illusions on the stabilisation of the world capitalist system, and also the hopes that capitalism could be restored in the USSR, whose economic development was proving the advantages of the planning system. Bourgeois economists could not ignore these circumstances, and in the 1930s the neoclassical concept gave way to Keynesianism, which maintained that capitalism, with its crises and mass unemployment, could be saved from a disastrous defeat in the contest with socialism only by the introduction of economic planning, with the capitalist state's vigorous intervention in the economy for the purpose of preserving private capitalist property.

The economic crisis of the 1930s forced the United States, the leading capitalist country, to look for opportunities to extend its exports through trade with the Soviet Union, and to establish diplomatic relations with the latter.

The collapse of capitalist society's relative stability and the deepening of its general crisis aggravated the contradictions between the imperialist powers in the struggle to redivide the world. It was these contradictions, and not the contest between capitalism and socialism, that led to the Second World War. Hitler Germany's aggression in a bid to realise the wild idea of a "thousand-year Reich of the superior German race" threatened not only Western Europe, but also the United States with colonial enslavement. Mankind was saved from fascist slavery, and civilisation from ruin and a return to barbarity, solely owing to the utter defeat of the fascist aggressors as a result of the Soviet Union's participation in the war.

The Second World War, unleashed by the most reactionary forces of imperialism, once again showed clearly that capitalism cannot ensure the development of the productive forces on the scale of the world economy. This historical mission can be performed only by the working class, the pivotal class of the epoch, which has risen from slavery to domination in a whole system of states united by socialist relations. The emergence of the socialist community as a result of the defeat of fascism, and the start of the disintegration of the colonial system of imperialism were a major feature of the second stage of the general crisis of capitalism.

At that stage, however, imperialism was still predominant in the world. The growing unevenness in the development of imperialist states turned the USA into a dominant force of the world capitalist economy. The USA rallied all the imperialist states in one military-political camp. As after the First World War, imperialist strategists and their ideological henchmen from among the bourgeois economists were again trying to prove that it was possible to hold back the development of the world revolutionary process and stabilise capitalism.

In its strategy, imperialism now counted both on economic and military strength. In its economic competition with socialism, capitalism hoped to realise the potentials of the incipient scientific and technical revolution. To stimulate scientific and technical progress, a new system of state-monopoly regulation of the economy was introduced in the developed capitalist countries, envisaging changes in its sectoral structure on the basis of "growth policy", with new industries growing faster than the traditional industries. Economic growth was presented as the most effective way to carry out social reforms and its goal was said to be the establishment of a "consumer society". Bourgeois economists tried to prove that in a "consumer society", allegedly free of economic crises and constantly increasing its wealth, it would be possible to integrate the working class into the system of state-monopoly capitalism and prevent the working-class movement from developing into a revolutionary class struggle.

In their struggle against socialism, the imperialists also counted on their military superiority. With the help of atomic and nuclear weapons and the virtually global system of military bases equipped with strategic aircraft targeted at the vital centres of the socialist countries, the United States at that time enjoyed the advantage of relative strategic invulnerability. This enabled it to lay claim to the role of world policeman in the struggle against the revolutionary forces.

These circumstances gave rise to illusions among bourgeois strategists and specialists in the world economy that capitalism had been stabilised, that communism could be "rolled back" and the world revolutionary forces defeated.

But the fundamental uniformities of world history relating to the economic competition between the two systems and ignored by bourgeois theorists manifested themselves with renewed force. In the second half of the 1950s, having blended the potentialities of the scientific and technical revolution with the advantages of its economic planning system, the Soviet Union was the first to enter the space age, and this altered the strategic situation in the world. The leading imperialist country had no alternative but to recognise the need for peaceful coexistence between the two systems. For the first time ever, prerequisites for the next stage of the general crisis of capitalism took shape in peacetime. At this new, third stage, socialism has gradually become the decisive force of world development.

The second half of the 1960s also saw the failure of the policy of integrating the working class into the system of state-monopoly capitalism on the basis of a "consumer society". State-monopoly measures to stimulate economic growth through deficit financing and vast outlays on militarisation led to runaway inflation, which reduced the real wages of workers and the incomes of sizable middle strata in town and country. In spite of continued economic growth, the developed capitalist countries were hit by grave socio-political crises. They were the scene of a powerful strike movement of the working people, who put forward political demands aimed against the whole system of state-monopoly capitalism.

Imperialist positions in the developing countries weakened. Having won political independence, the peoples of many of these countries continued fighting for economic independence. The national liberation movement was rising to a new stage in the struggle against all forms of exploitation, both precapitalist and capitalist. This changed the strategic situation on all the three continents of the so-called Third World. After the victory of the socialist revolution in Cuba, the anti-imperialist movement spread across a large section of Latin America. The suppression of the revolution in Chile dealt a heavy blow at this movement, but did not alter the balance of forces in favour of imperialism. In Asia, the defeat of US imperialism in Indochina gave a new impulse to the national liberation movement for a decisive attack on imperialism. In Africa, the racist-colonialist regimes in South Africa and

Rhodesia found themselves in even greater isolation with the fall of Portugal's colonial empire.

Imperialist positions were considerably weakened by the economic crisis of 1974-75, which for the first time since the 1930s spread virtually across the whole capitalist world. Its specific feature was that it coincided with an energy, raw material and ecological crises, and was coupled with the disintegration of the monetary system and with rocketing inflation, when the anarchy in the world capitalist economy was intensified to an uprecedented degree.

It was historical reality itself, with the general crisis of capitalism, that eroded the traditional foundations of bourgeois political economy.

3. The Crisis of Bourgeois Political Economy

So long as the Soviet Union was the world's only socialist state, there were no bourgeois theories of the international division of labour reckoning with the need for the long-term coexistence and contest between the two antagonistic modes of production. Bourgeois economists believed that socialism, surrounded by capitalist countries, was doomed. Even the most far-sighted bourgeois economists did not envisage the possibility of its playing an active role in the transformation of the whole system of the international division of labour. Bourgeois concepts of stabilising capitalism were largely confined to the national framework. It was only during the Second World War, which showed the inevitable prospect of gigantic upheavals in the whole capitalist system owing to the Soviet Union's decisive role in defeating fascism, that bourgeois political economy was faced with the need to formulate new concepts of world development. It concentrated on the problem of overcoming the contradictions within the world capitalist economy in order to prevent socialist revolutions and the drop-out of new countries from the imperialist system.

It was Keynes who formulated such a global concept for stabilising the capitalist economy, with a worldwide programme of state-monopoly regulation. As a vulgar economist proceeding from the exchange concept, he believed that to save capitalism from revolutionary upheavals it was necessary right after the war to set in motion the machinery for regulating monetary relations, international credit and world trade.

Recalling the stabilisation of the Deutsche Mark under the Dawes Plan after the First World War, Keynes was primarily concerned about the fact that towards the end of the war the capitalist states should set up a system of international mutual assistance to provide financial and material resources for suppressing the revolution first in Western Europe and then in other regions. Keynes's ideas were embodied in the International Monetary Fund (IMF), the International Bank for Reconstruction and Development (IBRD) and the General Agreement on Tariffs and Trade (GATT) which were set up as specialised UN agencies.

The very formation of the United Nations Organisation with the Soviet Union taking part as a victor power with a permanent place on the Security Council, which takes its decisions on the principle of unanimity, implied recognition of the need not only for coexistence between the two systems, but also for cooperation after the war.

But so long as imperialism enjoyed economic and military superiority, bourgeois concepts of the international division of labour ignored the need for cooperation between the two systems. Moreover, they started from the assumption that the UN and its specialised agencies should be used as an instrument of state-monopoly regulation of the world capitalist economy in order to ensure the gradual "erosion of socialism" and the involvement of the developing countries in the international capitalist division of labour.

However, as the socialist community grew stronger and colonial empires disintegrated, the UN could not be used as a superstructure of the world capitalist economy. In spite of imperialist opposition, the UN changed along lines which reflected the objective specific features of the new structure of the world economy. Its membership increased largely under the influence of the uniformities of the world revolutionary process not envisaged in the bourgeois concepts of the international division of labour. The evolution of these concepts in view of the need to adjust to the new situation in the world is most instructive.

Keynes's above-mentioned programme, which influenced the formation of the specialised UN agencies, was based on the decisive role of British-US imperialism in reorganising the world capitalist economy. The large loan granted by Washington to Britain in 1946, which was negotiated by Keynes, was an act of the state-monopoly export of US capital to Europe, which subsequently led to the Marshall Plan and created the prerequisites for imperialist integration. The ultimate goal of US-encouraged imperialist integration was to mould an Atlantic alliance as a single military-economic bloc incorporating all the developed capitalist countries.

The Keynesian policy of exporting capital to the former colonial and semi-colonial countries helped to shape a major line of imperialist economic strategy, which became an organic element of neocolonialist policy.

But imperialist ideologists and statesmen were unable to follow a common strategy in regulating the international division of labour and to rule out the world socialist system's active influence on this process.

Interimperialist contradictions were the main obstacle in the way to such a common strategy.

Since capitalism develops unevenly, instead of one power centre in the capitalist world, which took shape under US hegemony, there emerged three power centres: the United States, Western Europe and Japan. It was no longer possible to regulate the world capitalist economy from a single centre. Under the pressure of capitalist competition, the West European countries and Japan refused to play the role assigned to them by Washington. They violated the agreement on the economic blockade of the socialist countries and took the road of developing economic ties with these countries, envisaging not only broader trade, but also long-term cooperation projects. As a result, the pressure of capitalist competition served to aggravate the contest between the United States and its partners for the new and promising market in the socialist countries, whose stability is guaranteed by the planning system.

What made it impossible for Washington to regulate the global capitalist economy was not only the emergence of three power centres, but also the formation within it of yet another force that could not be controlled from a single centre: the multinational corporations, which even juridically were no longer subject to the control of individual capitalist governments. In their exterritorial economic "empires" incorporating dozens of states, the multinationals are guided solely by their own selfish interests of profit-seeking, so enhancing the anarchy in the world capitalist economy. The multinationals put into effect the most plunderous colonialist plans, dismissing the hypocritical promises of "aid" lavished on the developing countries by neocolonialist apologists. At the same time, some of the multinationals, reckoning on the strength of their market strategy, were quicker than the governments of the host countries to realise the profitability of orders from the socialist states, and have been using their own resources to credit such deals.

So, in spite of the wishes of the imperialist forces, the socialist countries are playing an ever more important role in the international division of labour with the developed capitalist countries; without this, it would have been impossible to carry on the reproduction process in an ever wider range of industries.

The imperialist attempts to isolate the socialist countries from the young national states have proved to be even more futile. This was the area where the bourgeois theories of the international division of labour failed first of all.

The models of economic growth offered to the developing countries by bourgeois theorists from the former metropolitan countries were purely technocratic, and did not envisage any meaningful socio-economic transformations. Naturally, the attempts to perpetuate the vestiges of slavery and feudalism in the developing countries were resisted by the national liberation movement, which involved ever broader sections of the population. Objective economic and political uniformities urged the masses to fight for a break with imperialist military blocs, for ousting the multinationals from the key sectors of the economy, and for the non-capitalist road of development, which opens up opportunities for radical socio-economic transformations.

Assistance from the socialist states made it possible for the former colonial countries to take part in the international divison of labour on an equal footing.

So, both the uniformities of the general crisis of capitalism and the logic of the world revolutionary process called not only for peaceful coexistence, but also for mutually advantageous long-term cooperation between the two systems. At the turn of the 1960s, it also became necessary for the two systems to cooperate in the solution of vital problems facing the whole of mankind and engendered by the random forces of market competition that are in play in the world capitalist economy. Among these problems was the urgent need to end the race in nuclear weapons and stop their proliferation, to overcome the dangerous consequences of the violation of the global ecological balance, and to solve the world food problem. The socialist countries launched an active campaign to solve these vast problems on the basis of cooperation between the two systems, opening up totally new prospects for the international division of labour.

Realisation of the Peace Programme adopted by the 24th Congress of the CPSU and further elaborated by the 25th Congress acquired exceptional importance in the early 1970s, in view of the deep-going changes in the development of the general crisis of capitalism. The Peace Programme formulated in concentrated form the objective tendencies of global historical development conditioned by the victories of socialism and the world revolutionary forces as a result of the economic competition between the two systems, which has paved the way for qualitative changes in the development of the productive forces on the scale of the whole planet and in the interests of the whole of mankind.

The realisation of the Peace Programme, whose aim is to make peaceful coexistence and mutually advantageous cooperation between the two systems irreversible, has in the first place created a practical basis for ruling out world wars from the life of society and gradually ridding the peoples from the grave burden of the arms race. The first step in this direction was the agreement on limiting nuclear-missile weapons, which should be followed up with measures to reduce conventional arms and to use the funds released as a result of cuts in the military budgets of developed states as aid to the developing countries.

The Peace Programme substantiates the possibility of developing the world economy on the basis of the international division of labour, peace and friendship among all nations of the planet.

Formation of conditions for the rational use of resources and development of the productive forces on a global scale is a task which capitalism could not even formulate. The socialist countries' initiative in this respect shows the decisive role of the new relations of production for the development of the modern productive forces. The fact that capitalism can no longer openly reject such a programme, and that the initiative in its implementation is in the hands of the socialist forces is due not only to the deepening general crisis of capitalism, but also to the bankruptcy of bourgeois economic doctrines of world development.

International detente, however, is only a tendency of development, which is at cross-purposes, so long as imperialism exists, with a counter-tendency. Imperialism has not laid down its arms, especially in the ideological struggle. Bourgeois theorists, while recognising the principle of peaceful coexistence, have recently devoted special attention to a theoretical renewal of their anti-communist doctrines. Petty-bourgeois ideologists are also helping them in this endeavour.

As it was pointed out at the 26th Congress of the CPSU,

> "the policy of peaceful coexistence charted years ago by Lenin is exercising an increasingly decisive influence on present-day international relations. The seventies have shown this convincingly." [1]

Marxists-Leninists have vigorously criticised bourgeois and petty-bourgeois political economy in order to accelerate the revolutionary transformation of

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[1] L. I. Brezhnev, *Report of the Central Committee of the CPSU to the XXVI Congress of the Communist Party of the Soviet Union and the Immediate Tasks of the Party in Home and Foreign Policy*, Novosti Press Agency Publishing House, Moscow, 1981, pp. 34-35.

the world in the interests of the whole of mankind. One of the most powerful instruments in this ideological struggle is the Marxist-Leninist theory of the general crisis of capitalism, which brings out the objective laws leading to the collapse of the imperialist structure of the world economy, the uniformities of the world revolutionary process, and the role of the economic contest between the two systems in building up a world economy based on planned and balanced use of the Earth's resources in the conditions of peace and friendship between all states and nations.

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The Reading Generation

1960 جي ڏهاڪي ۾ عبدالله حسين ” اُداس نسلين“ نالي ڪتاب لکيو. 70 واري ڏهاڪي ۾ وري ماڻڪَ ”لُڙهندڙ نسُل“ نالي ڪتاب لکي پنهنجي دورَ جي عڪاسي ڪرڻ جي ڪوشش ڪئي. امداد حُسينيءَ وري 70 واري ڏهاڪي ۾ ئي لکيو:

انڌي ماءُ ڄڻيندي آهي اونڌا سونڌا ٻارَ
ايندڙ نسل سَمورو هوندو گونگا ٻوڙا ٻارَ

هر دور جي نوجوانن کي اُداس، لُڙهندڙ، ڪَڙهندڙ، ڪُڙهندڙ، ڀَرندڙ، ڀُرندڙ، ڪِرندڙ، اوسيئڙو ڪندڙُ، ياڙي، ڪاٺُو، ياڄوڪڙُ، ڪاوڙيل ۽ وِڙهندڙ نسلن سان منسوب ڪري سگهجي ٿو، پَر اسان اِنهن سڀني وچان ”پڙهندڙ“ نسل جا ڳولائو آهيون. ڪتابن کي ڪاڳر تان کڻي ڪمپيوٽر جي دنيا ۾ آڻڻ، ٻين لفظن ۾ برقي ڪتاب يعني e-books ناهي ورهائڻ جي وسيلي پڙهندڙ نسل کي وَڌڻ، ويجهڻ ۽ هِڪ ٻئي کي ڳولي سهڪاري تحريڪ جي رستي تي آڻڻ جي آسَ رکون ٿا.

پڙهندڙ نَسل (پَنَ) ڪا بہ تنظيمَ ناهي. اُنَ جو ڪو بہ صدر، عُهديدار يا پايو وِجهندڙ نہ آهي. جيڪڏهن ڪو بہ شخص اهڙي دعوىٰ ڪري ٿو تہ پَڪَ ڄاڻو تہ اُهو ڪُوڙو آهي. نہ ئي وري پَنَ جي نالي ڪي پئسا گڏ ڪيا ويندا. جيڪڏهن ڪو اهڙي ڪوشش ڪري ٿو تہ پَڪَ ڄاڻو تہ اُهو بہ ڪُوڙو آهي.

جَهڙيءَ طَرَح وڻن جا پَنَ ساوا، ڳاڙها، نيرا، پيلا يا ناسي هوندا آهن اَهڙيءَ طرح پڙهندڙ نَسُل وارا پَنَ بہ مختَلِف آهن ۽ هوندا. اُهي ساڳئي ئي وقت اُداس ۽ پڙهندڙ، بَرندڙ ۽ پڙهندڙ، سُست ۽ پڙهندڙ يا وِڙهندڙ ۽ پڙهندڙ بہ ٿي سگهن ٿا. ٻين لفظن ۾ پَنَ ڪا خُصوصيِ ۽ تالي لڳل ڪِلَب Exclusive Club نہ آهي.

ڪوشش اها هوندي تہ پَنَ جا سڀ ڪَم ڪار سَهڪاري ۽ رَضاڪار بنيادن تي ٿين، پر ممڪن آهي تہ ڪي ڪم اُجرتي بنيادن تي بہ ٿِين. اهڙي حالت ۾ پَنَ پاڻ هِڪَبِئي جي مدد ڪَرڻ جي اُصولَ هيٺ ڏي وَٺُ ڪندا ۽ غيرتجارتي non-commercial رهندا. پَنَ پاران ڪتابن کي ڊِجِيٽائِيز digitize ڪرڻ جي عَملَ مان ڪو بہ مالي فائدو يا نفعو حاصل ڪرڻ جي ڪوشش نہ ڪئي ويندي.

ڪتابن کي ڊِجِيٽائِيز ڪرڻ کان پوِ ٻيو اهم مرحلو وِرهائڻ distribution جو ٿيندو. اِهو ڪم ڪرڻ وارن مان جيڪڏهن ڪو پيسا ڪمائي سگهي ٿو تہ ڀلي ڪمائي، رُڳو پَنَن سان اُن جو ڪو بہ لاڳاپو نہ هوندو.

پَنَن کي کُليل اکرن ۾ صلاح ڏجي ٿي تہ هو وَسَ پٽاندڙ وڏِ کان وَڏِ ڪتاب خريد ڪَري ڪتابن جي ليکڪَن، ڇپائيندڙن ۽ ڇاپيندڙن کي هِمٿائِن. پر ساڳِئي وقت عِلم حاصل ڪرڻ ۽ ڄاڻ کي ڦهلائڻ جي ڪوشش دوران ڪَنهن بہ رُڪاوٽَ کي نہ مڃن.

شيخ اَيازَ علمَ، ڄاڻَ، سمجهہَ ۽ ڏاهپَ کي گيتَ، بيتَ، سِٽَ، پُڪارَ سان تَشبيهہ ڏيندي انهن سينني کي بَمن، گولين ۽ بارودَ جي مدِ مقابل بيهاريو آهي. اياز چوي ٿو تہ:

گيتَ بہِ ڄڻ گوريلا آهن، جي ويريءَ تي وار ڪَرن ٿا.

... ...

جٿئن جٿئن جاڙ وڏي ٿي جَڳَ ۾، هو بوليءَ جي آڙ ڇُپن ٿا؛

ريتيءَ تي راتاها ڪن ٿا، موٽي مَنجهہِ پهاڙ ڇُپن ٿا؛

... ...

ڪالهہَ هُيا جي سُرخ گُلن جيئن، اڄڪلهہ نيلا پيلا آهن؛

گيتَ بہِ ڄڻ گوريلا آهن........

... ...

هي بيتُ اَٿي، هي بَم- گولو،

جيڪي بہ ڪٽين، جيڪي بہ ڪٽين!

مون لاءِ ٻنهي ۾ فَرَقُ نہ آ، هي بيتُ بہ بَمَ جو ساٿي آ،

جنهن رِڻَ ۾ رات ڪَيا راڙا، تنهن هَڏَ ۽ چَمَ جو ساٿي آ ـ

اِن حسابَ سان اٽڃاٽائي کي پاڻَ تي اِهو سوچي مَڙهڻ تہ ”هاڻي ويڙهہ ۽ عمل جو دور آهي، اُن ڪري پڙهڻ تي وقت نہ وڃايو“ ناداني‎ءَ جي نشاني آهي.

پَنَ جو پڙهڻ عام ڪِتابي ڪيڙن وانگر رُڳو نِصابي ڪتابن تائين محدود نہ هوندو. رڳو نصابي ڪتابن ۾ پاڻ کي قيد ڪري ڇڏڻ سان سماج ۽ سماجي حالتن تان نظر ڪڇي ويندي ۽ نتيجي طور سماجي ۽ حڪومتي پاليسيون policies اٽڄاڻن ۽ نادانن جي هٿن ۾ رهنديون. پَنَ نِصابي ڪتابن سان گڏوگڏ ادبي، تاريخي، سياسي، سماجي، اقتصادي، سائنسي ۽ ٻين ڪتابن کي پڙهي سماجي حالتن کي بهتر بنائڻ جي ڪوشش ڪندا.

پڙهندڙ نَسُل جا پَنَ سيني کي **چو، ڇالاءِ ۽ ڪيئن** جهڙن سوالن کي هر بَيانَ تي لاڳو ڪرڻ جي ڪوشَ ڏين ٿا ۽ انهن تي ويچار ڪرڻ سان گڏ جوابَ ڳولڻ کي نہ رڳو پنهنجو حق، پر فرض ۽ اٽٽر گهرج unavoidable necessity سمجهندي ڪتابن کي پاڻ پڙهڻ ۽ وڌ ڪان وڌ ماڻهن تائين پهچائڻ جي ڪوشش جديد ترين طريقن وسيلي ڪرڻ جو ويچار رکن ٿا.

توهان بہ پڙهڻَ، پڙهائڻ ۽ ڦهلائڻ جي اِن سهڪاري تحريڪ ۾ شامل ٿي سگهو ٿا. بَس پنهنجي اوسي پاسي ۾ ڏِسو، هر قسم جا ڳاڙها توڙي نيرا، ساوا توڙي پيلا پن ضرور نظر اچي ويندا.

وڻ وڻ کي مون ياڪي پائي چيو تہ ”منهنجا ياءُ
پهتو منهنجي من ۾ تنهنجي پَنَ پَنَ جو پڙلاءُ“.
- اياز (ڪلهي پاتم ڪينرو)