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A THEORIST'S COMMENT ON THE CURRENT BUSINESS CYCLE

I.

For the sake of clearness we begin by the following definitions:

Statistically the term "cycle" means two things: first that sequences of values of economic quantities in historic time (as distinguished from theoretic time) do not display monotonic increase or decrease, but (irregular) recurrence of either these values themselves or their first or their second time-derivatives. Second, that these "fluctuations" do not occur independently in every such time series, but always display either instantaneous or lagged connection with each other.

Statistically we mean by the word "trend" the fact that in many, although not in all such time series, it is possible to divide the whole interval covered by our material into sub-intervals such that the mean values of the time integrals over these sub-intervals are constantly increasing or decreasing as we go along in time, or that they display recurrence only once.

By "outside disturbance" we mean the action on the economic system of factors other than those which come within the sphere of business behavior as usually understood. In this sense not only wars, revolutions, natural catastrophes, institutional changes, however much they may have to do with economic situations, but also changes in commercial policy, in banking and currency legislation

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and habits, variations of crops as far as due to weather conditions and so on, are all outside disturbances.

We distinguish between particular, aggregative and general equilibria. The last-named we define by reference to the Walrasian system. Although in reality economic life never reaches this state, it is yet a fact that it sometimes draws away from it and sometimes draws towards it. Hence there are points on our graphs of time series which are nearer to it than any others. Owing to the presence of lags and so on, these points do not in different time series occur at exactly the same dates. Time intervals in which such points occur in a majority of time series, we call neighborhoods of equilibrium (which therefore are not neighborhoods in the mathematical sense).

Cycles necessarily lie between neighborhoods of equilibrium. In the pure model of economic change they have only two phases. But owing to the fact that depressive forces ~~guide their~~ Sets momentum on the way back from the prosperity excursion of the system, the latter usually outruns the first neighborhood of equilibrium it strikes and embarks upon a depression phase, from which it is forced up ~~again~~ by the action of the equilibrium ligamina and brought back again to another neighborhood from which the prosperity of the next cycle starts. Hence we, as a rule, have four phases, prosperity, recession, depression and revival. This is now almost generally recognized,

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but it is important to note that for purposes of fundamental analysis we are not free to count cycles from any point or phase we please, for instance from peak to peak or trough to trough, but must always begin after the revival and at the beginning of a prosperity. It is, moreover, essential to distinguish these two, although it may be difficult to do so, owing to the fact that they are both positive. The failure to do so, and especially to recognize that the "forces" at work in revival are entirely different from the "forces" at work in prosperity, is one of the main sources of faulty analysis.

Whatever starts a deviation of the system from equilibrium always, although not with logical necessity, gives rise to secondary phenomena which are mainly due to the fact that business men will act on the rates of change they observe. The sum total of these induced phenomena which are the centre of the mass psychology of cycles and greatly intensify their amplitudes, we call "secondary waves". The expression, first used in 1911, is misleading and is kept only because Mr. Keynes has taken it up. But the thing is very important, so much so that the majority of students of the business cycle see nothing else. Whilst this accounts for many errors in diagnosis and remedial policy, it also helps to explain and partly to justify a large group of "theories" which, though missing the essential phenomenon, are yet perfectly satisfactory when viewed as descriptions of part of the mechanism of

the secondary waves superimposed on the primary ones.

By "growth" we mean changes in economic quantities which occur continuously in the sense that the annual increment or decrement can as a rule be currently absorbed by the system without perceptible disturbance of equilibrium. Increase of population is the outstanding example.

Finally, by "innovations" we mean changes in production functions which cannot be decomposed into infinitesimal steps. It should be observed, however, that whilst it seems necessary to stress the element of discontinuity for some of the "microscopic" purposes of economic theory, among them the study of business cycles, there is much to recommend, especially for the purposes of broad historic survey, a "macroscopic" view to which the economic process in time may well appear as continuous for many centuries together.

II.

Although outside disturbances act so frequently and so powerfully on our material that almost any fluctuation could without absurdity be traced to one of them, there is nevertheless both scientific interest and practical point to an attempt to set up a model of economic change in time under the assumption that such disturbances are absent, and to see how much of actual fact it will satisfactorily account for. We shall therefore do this ~~in dealing with this~~ most important chapter of any complete

neglect that

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business cycle, which probably accounts for the greater part of the events which are responsible for the popular picture of the phenomenon in the public mind. For shortness' sake we also neglect the element of growth, which is non-cyclical anyhow and would be very small in the absence of more important factors of change.

What remains is a process of economic change in time which consists of the insertion into the economic system of new things or new ways of doing things, new products, new methods of production, and so on, and the elimination of what becomes unadapted thereby. Obviously this is a physiological and not a pathological process. What we have said so far did not involve any hypothesis and was merely a conceptual formulation of facts, but propositions in explanation of the further fact that that process goes in cycles do involve hypothesis, however well they may be founded on statistical and historical fact. We do not go into this, but confine ourselves to the assertion of the presence of an association between cyclical movements and industrial change, which is borne out by overwhelming evidence and may be followed up by anyone who prefers the monetary ~~outside~~ surface to the industrial essence by reference to the process of investment. The only thing we have to add and which is also a fact is that industrial change consists of a vast multitude of interacting ~~indefinite~~ processes of very different importance and span, and that linking it up with the

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cycle unavoidably means the recognition of the presence of many cyclical movements going on together, superimposed on each other, interfering with each other. Of course we may nevertheless, in order to secure the maximum of simplicity, try to describe that multitude statistically on the expository postulate that there is only one single cycle. This postulate works quite well, and the present writer even wishes to withdraw criticism of Professor Mitchell's work offered a few years ago. But we must beware of interpreting such procedure to mean a single-cycle theory and we must expect it to produce discrepancies with facts which may become important as we penetrate deeper and deeper into details. We therefore prefer a descriptive hypothesis to the effect that assuming three kinds of cycles will roughly account for the behavior of our material. Experience teaches that five cycles would work better. But our convention has the double merit of recognizing the multitude but confining work to manageable proportions. Historic substantiation is of course required in all cases. In order to convey our meaning quickly and to avoid the necessity of lengthy explanation, we shall call the three classes Kondratieff, Juglar and Kitchin cycles (as this, I suppose, will be understood by everybody), and confine ourselves to stating that as far as our own analysis shows at present each Kondratieff since the beginning of the eighties of the eighteenth century contains six Juglars of roughly nine to ten years' duration

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and each Juglar three Kitchins. Phases of the short cycle are occasionally nearly ironed out if they happen to coincide with a very marked opposite phase of the Juglar cycle, and the phases of the latter are sometimes substantially toned down for an analogous reason. Each class of cycles has its own neighborhoods of equilibrium of corresponding order, which with due caution may some day be linked up with the theoretical concepts of short, longer and longest period equilibrium.

It should be observed: first, that from the view outlined it is not irregularities but that much of regularity which we actually observe which calls for explanation. Of course the regularity of the schema must not be confused with an assertion of corresponding regularity in ~~effects~~ facts. What of correspondence between the two we observe has to stand on its own merits. Second, that any trend in the aggregates represented by our time series, as far as it is not due to growth, is not a distinct, real phenomenon due to a special set of causes, but simply the statistical expression of the cumulation of the net results of successive cycles. It is obvious therefore that it should go through the neighborhoods of equilibrium quite irrespective of how it will ~~then~~ cut through the material. We shall then have a succession of trends of various orders, the last and fundamental one going through those neighborhoods of the Kitchin and Juglar which coincide with the neighbor-

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hoods of the Kondratieff. It should finally be observed that such evidence as is for instance implied in the negative (if judged by the χ^2 test) result of A. B. Wilson's periodogram experiment is amply accounted for, not only by the presence of outside disturbances but also by what may be termed the inner irregularity of the phenomenon. Because of this, mere height or depth of peaks or troughs does not mean anything at all, even if occurring in a majority of our time series: There is no general rule by which we could tell, for instance, when a business community is going to lose its nerve in one situation rather than in another, and it may well do so and send down the indices in a spectacular way when fundamentally there is much less wrong with the particular situation than with another in which we observe nothing of the kind. All of which seriously limits the scope and usefulness of analysis by formal methods.

What we would reply to critics doubting the "existence" of the classes of cycles we are going to use is clear: They are merely names for certain groups of facts, and it is these facts which would have to be denied if the "reality" of, say the Kondratieff ~~is~~ were called into doubt, among them such things as the long swing of the price level.

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III.

Economic historians of the nineteenth century have unconsciously and independently testified to the reality of what statistical evidence induces us to call the Kondratieff cycle from about 1783 to about 1842. And they also bear out our theoretical interpretation of the phenomenon by having coined the now obsolete phrase of "the industrial revolution," which really implies everything we mean. Historians of the future will find little difficulty in recognizing the presence of an historic unit of a ~~singular~~ similar kind, the start~~ing~~ about 1897. As is to be expected, dates for different countries do not exactly coincide, and in the case of this country the political scare of 1896 blurs the contour of events. It is nevertheless easy to establish the claim of 1897 to being called a neighborhood of equilibrium of the highest order by reference to a dozen or so of our fundamental ~~theories~~ series and to the business history of the year. It would be interesting to discuss a number of other symptoms of "normality," such as the fact that hardly ever since the emergence of the modern state public finances have been in such perfect order in so great a number of countries as they were then: In many respects that year marks the high point of success of bourgeois society or of competitive capitalism. The innovations which disturbed its equilibrium stand unmistakably before our eyes and may be summarized by the words: electricity, chemistry, and motor cars. So ~~not~~ do the industrial and financial processes by which they were carried into effect and which account

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satisfactorily for the ensuing span of prosperity, which, however, did not last long. It is impossible to be quite sure about this, not only because of the World War but also because of the shadow which it cast years before the actual outbreak, and in fact ever since 1900. But the Kondratieff prosperity displayed symptoms of slackening down as early as 1911. If we dare to accept this, then it would have comprised about one and one-half Juglar cycles which, doubtless a chance coincidence, would exactly correspond to the simplest possible form of the three-cycle schema. The fifth Kitchin cycle was just about to turn into depression when the war broke out, the panic demand incident to which preventing what would otherwise probably have shown up as a major trough.

During this span all the familiar symptoms are present, among them the rise of prices (although it was a very gentle one if we disregard farm products) and of interest rates, of profits and of money wages, according to expectation also in most countries a much smaller rise in real wage rates, extensive spending on new plant, in most countries (especially in Germany) increasing strain on the financial engine. Deviations from the regulation course of events as postulated by theory can in every case be accounted for satisfactorily. Nor are the other symptoms absent, such as social unrest - for prosperity and welfare are very different and in some respects opposed phenomena. In this country inflation did not go far enough to suppress

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the regular pulse of the Kitchins, but inflation and deflation and, what ought to be self-evident but is consistently left out of account, the economic and social consequences of the war, stretching right into the economic mentality of the business man, who had learned to ~~rely~~ lean on the state, and into the actual (even where not legal) institutional framework of the economic process, introduce so many disturbing factors that no conclusion for the fundamental theory of the phenomenon ought to be drawn from this material alone.

But after the war we see a falling tendency in the price level which we can clearly distinguish from the effects of the descent from the peak of war inflation and which asserted itself even in countries where conscious effort was made to stop it. We also see a tendency for the rate of interest to fall, in spite of the effects of the devastations and excesses of the war which worked the other way, in spite also of political and social uncertainties which prevented that tendency from taking its free course. Moreover, we see that rapid increase in physical production which theory tells us is characteristic of long-time downswings and really means the harvest of the achievement of preceding upswings. Industrial change is of a type characteristically different from that of spans of prosperity: It consisted ever since the war not so much in the introduction of fundamentally new things, but rather of expansion, application and improvement

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in detail of what had been initiated before. The postwar time was, to use expressions from different theoretic frameworks, typically a time of "induced invention" and of "exploiting investment opportunity" potentially created before. Taylorization, improvement in organization and in the handling of materials, elimination of obselete and inefficient plants or firms, the intrusion of new things into the domain of old ones and the competing out of life of the latter, fit into the picture, as does the pressure of supernormal unemployment, although the latter has been much intensified by other reasons. Relying on the common knowledge of all these things, we may say that the period is in all respects analogous to what was called the "Great Depression" - 1873-1896.

This is what we mean by saying that we are (and have been for probably about twenty years) in the down-grade of the current Kondratieff cycle, and if it be permissible to say so with due reserve, in its third or depressive phase, which may be expected to run on for some time. Applying our schema once more, and once more asking the reader to bear in mind our meaning of such a statement and no other, we might make bold to say that we are in the revival phase of the fourth Juglar of the current Kondratieff. Of course this means generalizing mere statistical evidence and assuming irregularities which not only experience but also theory tells us we must not too confidently expect. The only motive for making such statements

is that they are a convenient expression of facts and are helpful in analysis as well as misleading.

IV.

Although some of our most important postwar series, such as the department store sales (Federal Reserve Board Index) or the Dodge figures for building contracts, did not reach their low until 1933, most of the fundamental ones did so in the summer of 1932, at all events in this country, but also in some others. And 1933 averages higher in most of even those cases in which the low occurred in that year. For instance, the earnings of department and specialty stores displayed a strong reversal of tendency for 1933, and the gross margins in the case of department stores were even, if we trust a sample (Harvard Bureau of Business Research, Bulletin No. 92), above those of 1929. Various factors, prominent among which is politics, combine to make it impossible to rely entirely on this evidence, the factual side of which is probably not contested. If we may accept it we should say from our standpoint that the summer of 1932 came to lie on a depression of the fourth Juglar, which did not turn into revival before the first months of 1934. But according to our schema the second short cycle of this Juglar, which had been in its depression phase during the last months of 1931 and about the first half

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of 1932, entered upon its revival phase somewhere in the summer of 1932. This revival lasted into 1933, to turn into the prosperity phase of the third short cycle somewhere in the first half of that year. Recession in this cycle set in during 1934, but ~~encroaching~~ impinging upon the revival phase of the Juglar did not assert itself as much as the recession of its predecessor. The same should hold true for the ensuing depression phase, whilst the final revival should be intensified by coincidence with the Juglar revival. All of which could be expressed just as well in terms of universally recognized commonsense business fact.

What has been said and the inference to be drawn from it ~~are~~ is of course subject to the element of outside disturbance, which, if sufficiently persistent, may well destroy the mechanism on which we have reasoned. For this reason alone if for no other, no prediction about actual events can be confidently made, at least not in any other sense than that of a statement of present and past fact which would have certain future consequences if nothing interfered with it. Outside disturbances do not come within the compass of this paper. Only insofar as some of them also disturb the behavior of important time series, which therefore might be the starting-point of objections to the analytic model underlying this sketch, it is necessary to point out that the stubborn resistance to the tendency of the price level and money rates of wages to fall is

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not only responsible for both the sham stability of the period 1923-1929 and the severity of the breakdown but from the nature of the practices adopted also for an abnormal behavior of the series of adjusted demand deposits and others. It is therefore relevant to observe that in a section of the Middle West into which the effects of Federal Reserve policy did not penetrate with full force, the deposit figure marks the recessions of 1924 and 1927 exactly as it should. The behavior of industrial profits, which also were abnormal, for a Kondratieff down-grade, is perfectly accounted for by the effects of the idea that the price level should be kept constant and by a public mentality which in order to ~~exist by~~ maintain living on uncritical hopes for the future hardly needed that additional inducement which was supplied by a most curious relapse of monetary theory into pre-scientific habits of thought, some of them clothed in the most modern technique available.

Ever since, in the sixties of the past century, Clement Juglar definitely established the existence of wavelike movements which pervade economic life within the institutional framework of capitalist society, the work of finding, marshalling, measuring relevant fact has been steadily progressing. Although much hampered by needless controversy and inadequate technique, this work has yielded results which it is believed need only be properly coördinated and developed in order to enable economics to offer a substantially satisfactory and reasonably exhaustive picture of the phenomenon, and thus to make what would certainly be its most immediately practical contribution to human welfare. Coördination is particularly necessary of the historical, statistical and analytical modes of approach which are each of them thwarted by that reluctance to coöperation incident to the differences in training, tastes and horizon of individual workers. The purpose of this paper is to explain the main features of an analytic apparatus which may be of some use in marshalling the information we have and in framing programs for further research.

Outside Factors. If we survey, for instance, the course of economic events in England from the beginning of the French Wars in 1792, through the suspension of specie

payments, the Peace of Amiens, the trade war with America, up to the crisis in 1809-1810, it becomes obvious that we could without any glaring absurdity account by political "disturbances" for all the fluctuations we observe in our material. Or if we follow the course of the world crisis through the spring of 1931, we may trace the breakdown of the distinct upward movement observable at the beginning of that year to a string of events arising out of the flutter caused by the reopening of the question of the union of Austria to Germany and the movements of short balances incident thereto. Commonsense immediately suggests that we have discovered an obviously important source of economic fluctuations. From the ubiquity of such events it follows that practically every economic fluctuation must be a historic individual and cannot be made amenable to explanation but by minute historical analysis of the innumberable factors actually at work in each case. In other words, in order to understand business cycles we must first of all acquire what may be termed historical experience of the way in which economic life reacts to such disturbances, and this is one of the reasons why every conquest of past fact is of paramount practical importance, in some respects of greater importance than additions to our stock of contemporaneous fact which can increase our knowledge over time only by infinitesimal steps. The statistical and analytical description of the various mechanisms of reaction (with a hope in our minds that we may ultimately get as far as to be able to measure

the effects attributable to every such disturbance) seems thus to be the most urgent task before us. It should be observed in passing that for various reasons any influence acting on the economic process is practically sure to produce not a single dent but a wavelike motion extending over longer time than it takes to reach the next disturbance, as well as, if it impinges on a particular spot, a vibration throughout the whole system. Adaptation proceeding almost always with a lag and very often with reference to the rate of change of the relevant quantities rather than to their absolute magnitude, our attempts at exact description are more than likely to result in expressions admitting of periodic integrals.

This being so, the question arises whether there are any fluctuations which arise out of the behavior of business communities as such and would be observable even if the institutional and natural framework of society remained absolutely invariable. Although disturbance of the kind glanced at and reaction thereto may in individual cases be much more important, yet the presence or absence of a fluctuation inherent to the economic process in time is practically and scientifically the fundamental problem and the only one to be considered here. In order to make headway with it, we shall proceed as physical sciences do in those cases in which it is impossible actually to isolate a phenomenon by producing it in a laboratory: from our historic knowledge and everyday knowledge of historic behavior we shall construct a "model" of the economic process over

time, see whether it is likely to work in a wavelike way, and compare the result with observed fact. Henceforth therefore we shall disregard not only wars, revolutions, natural catastrophes, institutional changes, but also changes in commercial policy, in banking and currency, legislation and habits, variations of crops as far as due to weather conditions, changes in gold production as far as due to chance discoveries, and so on. These we call outside factors. It will be seen that in some cases it is not easy to distinguish them from features of business behavior. All we can do about this here is to recommend the reader to hold tight to the commonsense of the distinction and to consider that every business man knows quite well that he is doing one kind of thing when ordering a new machine and another kind of thing when he is lobbying for an increase of the import duty on his product. It will also be seen that many of the things we list as outside factors are when considered on a higher plane and for a wider purpose, the direct outcome of the working of the capitalist machine and hence no independent agencies. This is surely so but does not reduce the practical value of the distinction on our plane and for our purpose.

Cycles, Trends, Equilibria, Growth, Innovation.

For shortness' sake, we assemble in this section a few necessary definitions and propositions, which are perfectly simple although we cannot help adding here and there

somewhat pedantic formulations which are necessary in order to convey to the specialist a perfectly precise meaning.

Statistically the term "cycle means two things: first that sequences of values of economic quantities in historic time (as distinguished from theoretic time) do not display monotonic increase or decrease, but (irregular) recurrence of either these values themselves or their first or their second time-derivatives. Secondly that these "fluctuations" do not occur independently in every such time series, but always display either instantaneous or lagged association with each other.

Statistically we mean by the word "trend" the fact that in many, although not in all such time series, it is possible to divide the whole interval covered by our material into sub-intervals such that the mean values of the time integrals over these sub-intervals are increasing or decreasing as we go along in time, or that they display recurrence only once.

The Three-Cycle Schema. The above analysis not only accounts for the fact that waves of prosperity always do arise whenever a neighborhood of equilibrium is reached and that they always do taper off into a new neighborhood of equilibrium, but as far as the present writer is able to make out, for every single fact or characteristic ever proved to be associated with either upswings or downswings not provably due to the action of outside factors. The reader is invited to make the experiment by drawing up a list of what he considers these characteristics to be and observing whether they fit into the model. But there is no reason to believe that there should be just a single wavelike movement pervading economic life. On the contrary it stands to reason that some processes covered by our concept of innovation must take much longer time than others to have full effect. The railroadization or electrification of a country, for instance, may take between one half and the whole of a century and involve fundamental transformations of its economic and cultural patterns, changing everything in the lives of its people up to their spiritual ambitions, while other innovations or groups of innovations may arise and disappear within a very few years. Moreover the former will generally be carried out in distinct steps and thus give rise both to shorter fluctuations and longer underlying swells. Under these circumstances it is not the most natural thing to assume the existence of a single cycle and to

postulate that it will display any very marked regularities. This is in fact a very bold hypothesis which could be justified only if clearly imposed upon us by our material. But as this is clearly not the case, even apart from what we may reasonably attribute to the outside disturbances to which our material is subject, it seems much more realistic (and also likely to do away with some spurious irregularities, that is to say, irregularities which are only due to the single-cycle hypothesis) to admit that there are many cycles rolling on simultaneously and to face squarely the problem of analyzing their interference with each other. As, however, it is necessary for the purpose of handling our time series to settle on a moderate number of distinct movements which may be thought of as superimposed to each other and passing their normals or neighborhoods of equilibrium near the points where they cross the path of the next higher cycle underlying them, the three-cycle scheme is here suggested as a fairly useful working hypothesis. Nothing more than descriptive merits are claimed for it, but it should be observed that it fulfills the one condition which a device of this kind may reasonably be required to fulfill - the condition of carrying historical meaning.

If we study, say, the economic state of things in all countries in 1872 and behold all the wild excesses of that boom, we shall have no difficulty in assigning very realistic meaning to the terms "want of balance" or "disequilibrium". Nor is it difficult if we look at things one year after to recognize that, however much the then situation differed from that of 1872, it was similar to it in that it was about equally unbalanced. Again, if we analyze the course of events in, say, 1897, we may well sum up the result by speaking of a comparatively equilibriated state of things. This commonsense distinction between comparatively balanced and comparatively unbalanced states of the economic system is of utmost importance for the description and measurement of cyclical phenomena. In order to bring out the exact skeleton of that observation we define: (Marshallian) particular equilibrium exists in an individual industry if this industry as a whole displays no tendency either to increase or decrease its output or the combination of productive factors it employs. Aggregative equilibrium exists if the sum total of receipts of business as a whole, expressed in current dollars, equals the sum total of costs similarly expressed and including as much profit as will induce everybody to keep on doing what he is actually doing. This kind of thing, which is compatible with plenty of disequilibrium as between industries and within industries, is the basic concept in Mr. Keynes' analysis of the monetary process. General equilibrium

exists if every household and every firm in the domain under research is individually in a state of equilibrium in the sense of Leon Walras. It is only this last concept that matters for us. To give it statistical meaning we must link it up with certain points on the graphs of our time series. These we call "normal points". As in reality such states can never be perfectly realized, we can be concerned only with states which are nearer to or farther from them than others. Hence we further define: neighborhoods of equilibrium are time intervals in which normal points occur in the graphs of our time series excepting those which in that interval are deflected by a definite and provable individual circumstance. (The word neighborhood is therefore not used here in its strict mathematical sense). Discussion of the question how we are to locate these neighborhoods cannot be entered upon in this article.

By "growth" we mean changes in economic data which occur continuously in the sense that the increment or decrement per unit of time can be currently absorbed by the system without perceptible disturbance. Increase of population, resulting in an increase of supply of labor of at most a few percent per year (historically an increase of three percent per year is already very high), is the outstanding example. If the factors which enter into this category were the only ones at work, there would be obvious economic meaning to the concept of trend and to its determination

by least squares or other methods resting on similar assumptions. In what follows we shall, however, not deal with the problems arising out of mere growth nor with the very complicated questions of their relation to the other types of factors in economic change. In fact we shall for clearness' sake disregard it altogether, which, as in the case of outside factors, does not imply any view about its importance.

It stands to reason, finally, that outside factors and growth factors do not exhaust the list of the influences which produce and shape economic change. Obviously the face of the earth would look very different if people, besides having their economic life changed by natural events and changing it themselves by extra-economic action, had done nothing else except multiplying and saving: if it looks as it does, this is equally obviously due to the unremitting efforts to improve according to their lights upon their productive and commercial methods, the changes in technique of production, the conquest of new markets, the insertion of new commodities, and so on. This historic and irreversible change in the way of doing things we call "innovations" and we define: innovations are changes in production functions which cannot be decomposed into infinitesimal steps - add as many mail-coaches as you please, you will never get a railroad by so doing.

It is a question of some interest why the old type of economist, Marshall included, should while

recognizing this element and taking account of it in special cases, yet have persistently refused to face it squarely and to build an analytic apparatus fully descriptive of its mechanism and consequences. For our purpose it is both necessary and sufficient to stress the necessity of listing innovation, however much it may be linked to the other two, as a third and logical distinct factor in economic change and to submit the propositions: the kind of wavelike movement which we call the business cycle is incident to industrial change and would be impossible in an economic world displaying nothing except unchanging repetition of the productive and consumptive process. Industrial change is due to the effect of outside factors, to the non-cyclical element of growth, and to innovation. If there be a pure economic cycle at all it can only come from the way in which new things in the institutional conditions of capitalist society are inserted into the economic process and absorbed by it. In fact it would have to be the statistical and historical form in which what is usually referred to as economic progress comes about. This is why any serious attempt at analytic and even at practical control of the business cycle would have to be an historical one in the sense that the key to the solution of its fundamental problems can only be found in the facts of industrial and commercial history.

Prosperity and Depression. To simplify argument we will in this section make the hypothesis presently to be discarded, that there is sense in speaking of one "cyclical movement" in our material.

We can of course never expect to discover a definite date when the first cycle arose out of a state of perfect equilibrium, but it is essential in order to avoid circular reasoning, to make our model describe such an event and as far as historical and statistical description goes, to make it start from what has first been identified as a neighborhood of equilibrium. We then get the picture of the system of economic quantities drawing away from this equilibrium or neighborhood under the impact of innovations which would supply, barring outside factors, the only possible "force". Let us visualize this by thinking of any of those booms in this country or in England which everyone would label as railroad booms. The new thing in this case takes years to get into working order and still longer to exert its full effects on the location of industry and agriculture, agglomerations of population, the volution of accessories and subsidiaries, and so on. During this time there would in strict logic and if the preceding equilibrium was a perfect one, be little or no increase in the stream of commodities and services (there may in fact be a decrease in the output of consumers' goods, while producers'

and consumers' expenditure would increase by credit creation and in other ways). The realistic complement of this is that during this period expenditure should regularly expand more than output and that the non-innovating factors of the economic system should adapt themselves to this state of things. It is not possible to show here by the historical interpretation of the behavior of time series (neither should it be necessary to show, for it must be obvious to everyone who has ever, e. g., studied the charts published in this Review) how perfectly this accounts for everything we mean when identifying a given interval as a time of business prosperity. After a period of gestation, which of course must be distinguished from what we designate by this term in the case of an individual firm, the products or services of the new business structures reach their markets, displacing either other such products and services or methods of production and concerns linked to them which have now become obselete, and forcing a process of liquidation, readjustment, and absorption. This would be so even if nobody ever made any errors and nobody every misbehaved, although there is no difficulty whatever in understanding that consequences of error and misbehavior will show up during this period in which the system struggles back to a new neighborhood of equilibrium. On the side of money and credit the fundamental element which induces all others is the fact that as soon as the receipts stream in from the sale of the new products and as far as they are used to pay back bank loans, deposits

will have to contract in strict logic down to the point of the previous neighborhood and in reality some way towards it. Again, there is no difficulty in inserting into this picture as understandable consequences of this fundamental chain of events, all the accidental phenomena which experience tells us are usually associated with it. This not only gives a truer picture of the nature and the organic functions of cyclical down-swings, but also accords satisfactorily with statistical evidence.

Whatever starts a deviation of the system from equilibrium always, although not with logical necessity, gives rise to secondary phenomena which are mainly due to the fact that business men will act on the rates of change they observe. The sum total of these induced phenomena which are the centre of the mass psychology of cycles and greatly intensify their amplitudes, we call "secondary waves". The expression, first used in 1911, is misleading and is kept only because Mr. Keynes has taken it up. But the thing is very important, so much so that the majority of students of the business cycle see nothing else. Whilst this accounts for many errors in diagnosis and remedial policy, it also helps to explain and partly to justify a large group of "theories" which, though missing the essential phenomenon, are yet perfectly satisfactory when viewed as descriptions of part of the mechanism of the secondary waves superimposed on the primary ones.

The units of the cyclical movements then lie necessarily between neighborhoods of equilibrium. In the

simplest form of the model of economic change they have only two phases. But owing to the fact that depressive forces gather momentum on the way back from the prosperity excursion of the system, notably owing to the phenomena incident to the breakdown of the secondary wave, the system outruns usually the first neighborhood of equilibrium it strikes and embarks upon a depression phase, from which it is forced up by the action of the equilibrium ligamina which bring it back again to another neighborhood from which the prosperity of the next cycle starts. Hence we have as a rule four phases, prosperity, recession, depression, and revival. This is almost generally recognized, but it is important to note that for purposes of fundamental analysis we are not free to count cycles from any point or phase we please, for instance from peak to peak or trough to trough, but must always begin after the revival and at the beginning of a prosperity. It is, moreover, essential to distinguish these two, although it may be difficult to do so owing to the fact that they are both positive. The failure to do so, and especially to recognize that the "forces" at work in revival are entirely different from the "forces" at work in prosperity, is one of the main sources of faulty analysis.

The fundamental question still remains unanswered. Why should the carrying into effect of innovations (as distinguished from invention or experimentation which are quite another matter and do not in themselves exert any influence

on business life at all, which is the reason why so little has come out of the Marshallian recognition of the element of invention) cluster at certain times and not be distributed in so continuous a way as to be capable of being equally continuously absorbed as the current increase in the supply of labor is? One answer suggests itself immediately: as soon as the various kinds of social resistance to something that is fundamentally new and untried ~~has~~ have been overcome, it is much easier not only to do the same thing but also to do similar things in different directions, so that a first success will always produce a cluster - see, e.g., the emergence of the motor-car industry. This is indeed the method of competitive capitalism which has not as yet died out in trustified capitalism to spread an improvement and to reap the social harvest - in the succeeding depression. But it would be necessary to go much deeper into this phenomenon, the roots of which stretch far beyond the economic field. As it has been the unfortunate experience of the present writer that even a very elaborate exposition failed to convey to critics the picture desired, he prefers to ask the reader to consider the clustering of innovations as a postulate or hypothesis made to fit the facts in the same way that such hypotheses are made in physics, irrespective of what might be adduced for or against their objective truths. But he feels entitled to say to anyone who doubts this

proposition: Look around you and see for yourself whether it is not so. Other writers have entirely independently stressed that fact that it is possible to associate historically every business cycle with a distinct industry or a few industries, which led in it and, as it were, applied the torch to what after becomes a flare-up covering a much wider surface. The well established fact that the fluctuations in investment goods are so much more marked than elsewhere points by virtue of its being explainable on the postulate mentioned, in the same direction.

It should be added that the above analytic model supplies an interpretation of economic trends which also bears on the technique of their determination. It follows, e.g., that barring the element of growth the trends of our time series are not due to influences distinct from those that create the cyclical fluctuations but simply embody the results of the latter. To these "result trends", as the writer calls them in his workshop, it is entirely unwarranted to apply formal methods of the type of least squares. For extrapolation there is of course no warrant in any case. But there are certain characteristics which may be used in developing formal methods as more or less rough approximations. No general proposition is possible as to the relative or absolute lengths of the four phases, even apart from the fact that they will be influenced by outside factors. Partly but not wholly for the latter

reason no great significance attaches to the mere height or depth of a peak or a trough although we shall presently find a reason for expecting that certain depressions will be much more severe than others.

which with material as exposed as ours is to disturbance by outside factors, which are not small, independent or "numerous" in the probability sense, is much more inportant than fulfillment of any formal criterion.

Historical knowledge of what actually happened at any time in the industrial organism and of the way in which it happened, reveals first the existence of what is often referred to as the "Long Wave" of a period of between fifty-four and sixty years. Occasionally recognized and even measured before, especially by Spiethoff, it has been worked out in more detail by Kondratieff, and may therefore be called the Kondratieff Cycle. Economic historians of the nineteenth century have unconsciously and independently testified to the reality of the first of these waves our material allows us to observe, with the cycle from about 1783 to 1842, and they also bore out in advance our interpretation of the phenomenon by coining the phrase of the industrial revolution, which really implies everything we mean: the phrase is infelicitous and justly considered obselete by now, but it pictures well how the happenings of the period struck entirely unprejudiced observers. 1842 to 1897 is readily interpreted as the age of steam and steel, particularly as the age of the railroadization of the world. This may sound superficial, but it can be shown in detail that railroad construction and work incident to it or connected with it or consequential upon it is the dominant feature both of economic change and of economic fluctuations during

that time and every one of the four phases into which it is possible to divide it. Future historians finally will find no difficulty in recognizing the initiating importance of electricity, chemistry and motor cars for both the up-swing and the down-swing of the third long wave, which rose about 1897. Of course if we prefer a more usual way of expressing the same thing we may put these processes also in terms of investment and the expansion and contraction of credit: this is certainly a very important part of the mechanism. Unfortunately this description is not only more usual but also more superficial and opens the door to all the crudities and errors of the various monetary theories of the cycle. Any satisfactory analysis of causes must start with what induces that credit expansion, as every satisfactory analysis of effects must start by investigating what is done with the increased monetary resources - after which we immediately cease to wonder why the mere increase of credit facilities in or before a depression proves as ineffectual as we know it does. If, however, we stop at the process of investment and postulate that it has a mechanism of its own, we do not only fail to get at the core of the matter but we also find it difficult to avoid such desperate logic as is implied in the conclusion that because increase of investment and expansion of credit are almost always associated with a prosperity phase, we can produce prosperity by expanding credit.

The majority of students of the business cycle does not consider the evidence alluded to sufficient to establish this particular cycle. But what does that mean? The term Kondratieff Cycle is for us but a name for a certain set of facts (a certain long-time behavior of the price level, the interest rate, employment, and so on), none of which is open to doubt. It is true that the term also implies an interpretation to the effect that this behavior of our series is amenable to interpretation on the same lines as their behavior in other cycles. But this again is merely an inference from historical facts which have not so far been called in question either. Of course experience of about two and three-fourth units of a phenomenon does not warrant much generalization and still less prediction. These, however, are very doubtful things in any case.

It is therefore only as a statement of fact that we venture to say that the two complete Kondratieff units within our range of statistical vision contain each of them six cycles of from nine to ten years' duration, equally well established by industrial history, though less clearly marked in our time series, which correspond as a matter of fact roughly to that cyclical movement which was the first to be discovered. Therefore we call them Juglar Cycles. As pointed out by D. H. Robertson, it is possible in every case to indicate the particular industry and the particular innovations which are responsible for the up-swing and the process of readjustment.

Finally, every Juglar so far observed (those of the present Kondratieff included) is, in most cases and readily in this country already by inspection, divisible into three cycles of a period of roughly forty months. Its existence has been pointed out repeatedly these hundred years or more, and still oftener has it been felt and recognized implicitly, but it was the two studies by Mr. Kitchin and Professor Crum in this Review that were chiefly instrumental in establishing it. Evidence about the commercial paper rate, this series being the most purely cyclical of all, is of course particularly important. That this cycle, as well as the others, are more clearly marked in this country than in any other and notably in England, is easily accounted for by the fact that cycles in most series will tend to be toned down or even ironed out the more a country's economic life is interwoven with international influence, and the more its policy approaches free trade. The question of the statistical methods which arise out of this analysis (for statistical methods must arise out of our understanding of the phenomenon they are to be applied to) will be taken up at another time. It is of course admitted not only that changes over time of another type also create wavelike movements but that besides the three just mentioned there are other cyclical waves. It is held, however, that the three-cycle scheme works sufficiently well for the purposes of the stage of rough approximations in which we are and are likely to remain for a considerable time.

A Research Program. If we coördinate available information, statistical and historical, in the light of the principles sketched out, we get not so much a picture as indications which give us an idea of what the real picture would be like. These principles do enable us to link up in a general way the behavior of those of our series which are most symptomatic of the pulse of economic life as a whole. These "systematic" series may be either synthetic, as for instance the series of price levels or of physical volume of production, or natural, as for instance series of interest rates, clearing-debits, unemployment, or, at least for the pre-war time, pig iron consumption, or of the sum total of deposits. They all, also in a general way, behave as they would have to if the general view outlined above were true to life. In the case of what by way of distinction from "systematic" we may call "individual" series, such as the prices and quantities of individual commodities, our analysis becomes more complicated and perfect knowledge of the particular conditions in every branch of industry and commerce, of its lags, frictions and inertias, of the mentality of its men, of its special randon influences to which it is exposed, and especially of its active or passive role in any given cycle, is necessary. As the outside factors impinge upon some phase of a process consisting of a number of superimposed wavelike movements, and as every one of these movements itself impinges upon a particular phase of some other

movement underlying it, so all of this impinges on the particular resonator in the case of every individual industry or firm, which responds according to its own structure. This is perhaps the best way of stating the problem in its full complexity, and infinitely helps to understand the many special cycles which some students have found or think they have found in many individual industries.

Now first not a single one of the systematic series represents adequately what it is meant to represent. And in no case is our historical or contemporaneous information adequate to account quantitatively for the fluctuations of the systematic series. It is only one side of the problem that this makes convincing verification of the result of any analysis impossible and that all we can do at present is to say that the testimony of such facts as we have is compatible or incompatible with it. The other side is that many questions are not questions of principle and analysis at all but simply of relative quantitative importance. The statement e. g. that in the down-grade of any cycle inertia of wages counts for something in determining the amount of unemployment, is too obvious to require proof; but not only for practical but also for scientific purposes this is entirely irrelevant as long as we are unable to say whether this element accounts for one percent or for ninety percent of the unemployment figure observed in a given place at a given time.

No wonder that if we are unable to be more precise than this, economics is considered as entirely useless by the practical man. Yet our analytic apparatus would turn out a definite answer all right provided the necessary factual information were inserted into it, the assembling of which is of course much beyond the means of any individual worker or private group of workers.

Seconly, there is no reliable information at all on a number of subjects which are obviously of primary importance. Two examples must suffice. Waiving our objection to the present tendency to overstress the importance of price levels and monetary magnitudes in general, we may say that the stream of expenditure by households on consumers' goods is one of the most indispensable elements in the analysis of the business cycle. We have acceptable though far from satisfactory indicators for the post-war time, but owing to the exceptional circumstances present in this period this is almost valueless for a fundamental understanding. And for the pre-war time we have to be content with payroll figures and the like, which might be easily misleading even if they went farther back than they do. Yet there is plenty of stray information stretching over centuries, which if it could be brought together would definitely clear up some of the most pressing practical problems.

Again, the process of investment and the corresponding process of credit contraction in down-grades can

never, whatever the theorist may say, be fully grasped in its importance and consequences until we know more about the relative importance of the sources and the actual behavior of borrowers and lenders. The decisive figure here is the sum actually spent on the production of durable producers' goods <u>for new purposes</u>. It is in these last three words that our chief difficulty lies which has so far been overcome only in a very few cases: we can follow up for instance how much was spent on railroad construction in England in the forties. It is difficult enough to find out how great the sum total that newly enters industry and trade every year. It is still more difficult to find how much of this is spent on equipment. But even this would not be enough. However, an investigation lighting up a very important side of the past and present of capitalist society would be perfectly feasible.

Although, third, the phenomenon of the cycle cannot be defined and understood as a sort of average between independent changes in individual industries, yet the behavior of individual industries, on the one hand causing and on the other hand responding to the sweep of changing business situations, requires a special study for each of them. Plenty of work has been done in that direction, but as the decisive questions have hardly ever been in the minds of the writers to whom we owe that literature of industrial monographs, the evidence is incomplete and inconclusive. There is hardly any event or peculiarity of

structural pattern in any industry which would be irrelevant to an explanation why the business cycle is what it is. Besides, if it be true that industrial change is at the bottom of the cyclical phenomenon, its mechanism can be established only by covering in detail all recorded cases of such change. A striking similarity reveals itself immediately to the first glance at such different processes as the rise of the English iron industry from the sixteenth to the end of the eighteenth century and the rise of the motor-car industry in our time. In these, as in many other cases, we have even now advanced much beyond general impressions, but there is a long way between this and the goal of establishing the validity of the schema of innovation and its monetary complement - copying the leaders - eliminating the obselete - pushing on into the new economic space opened up by the initiatory change and its consequences - and showing how it produces, together with its monetary complement, the particular kinds of waves inherent to the economic life of capitalist society and parallelled by similar phenomena in other fields of human activity.

"A Theorist's Comment on the Current Business Cycle"

Only those readers who are Conservative by or who have lived the Better part of their lives in Europe as who are more or less advanced in age can have an full appreciation that feeling of a landslide

[illegible] the feeling in the

self-supporting

(illegible)

Gedichtet th 24 II 48

I. For the orthodox socialist, the Comm Man. stands first in the list of the Sacred Writings of his Creed. Nor do I use "Creed" inadvisedly. One of the first things the detached student of Marxism discovers is that, sociologically, it is in the first neither a theory nor a program, but a Creed which is why it is so difficult to discuss [other socialisms?]

He, then, has plenty of reason to celebrate the Centenary. But what have we to do with it? At the beginning of Febr 48, just before the outbreak of the French Revol. of that year, but quite out of contact with it, two so-called German intellectuals, K. M. & F. E., issued a Manifesto, on behalf of a non-existing party, the Communist "Party" League (17 + 1852) that called itself a working-man assoc but was nothing but a loose group of intellectual desperadoes, exiles mostly from their countries.

Sept 47 gebor. Journal 3

The two authors advocated overthrow by force of all existing social structures - by concealed action in all countries - especially of the social system of private property and private econ. initiative

Engels, Nov 1850

Can capitalism survive
J.A.S. 1936

LECTURES IN CURRENT ECONOMIC PROBLEMS

A SERIES OF LECTURES WHICH WERE GIVEN IN THE U. S. DEPARTMENT OF AGRICULTURE GRADUATE SCHOOL IN COOPERATION WITH THE GRADUATE SCHOOL OF AMERICAN UNIVERSITY DURING 1935-36

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NOVEMBER, 1936

Can Capitalism Survive? Reprint and [illegible]

CAN CAPITALISM SURVIVE?

By
Josef A. Schumpeter
Harvard University

I. ~~In the opinion of the speaker the answer to the above question is in the negative.~~ But what counts in any such attempt at social diagnosis and prognosis is not the "Yes" or "No" by which we may sum up our facts and arguments but those facts and arguments themselves. They contain all that is scientific in the final result. Everything else is not science but prophecy. Strictly speaking, neither economics nor any other science ever foretells what will happen. To do this in a process which is the function of very many variables which are only partly amenable to exact measurement, would require super-empirical insight of the kind which is the very definition of prophecy. Economics or any other science can only state what would happen if a given process were allowed to go on in the same way as it did during the period from which we take the material for our analysis. This not only limits the scope of our subject but also bears upon it in a more direct way which may be pointed out at once: In the course of an argument presently to be entered upon, we shall draw conclusions about the future behavior of total output of commodities and services from the behavior of that quantity which we are able to observe in the past. There are several objections to this or any other extrapolation. At the outset we wish to mention but one of them: Owing to the failure of the conditions of the urn schema to be fulfilled, there is no sense in speaking of any "probable" future amount of total output, but our inability to justify any proposition on probability considerations does not mean that it therefore must necessarily lack any justification at all. If we fit a smooth function to any time series and extrapolate, the result need not have any forecasting value. As a matter of fact, in very many cases it is at once obvious that the expectation based on such a trend quickly leads to perfectly absurd results, but this means no more than that formal methods are not fool proof. If analysis teaches us that the trend expresses a real force or process which we have reason to believe will persist under certain conditions, there is no absurdity in extrapolating provided we keep in mind the above distinction between what will and what would happen.

Our question is indeterminate because of the many meanings one may attribute to the much abused word "capitalism" which indeed it would be best to banish from scientific terminology. Disagreement on our question is often due to this fact alone. One of the difficulties is the word must unavoidably designate different things according to whether we argue in terms of economic or sociological fact. We will define it as follows, stating expressly that this would be unsatisfactory for many purposes: Capitalism is that organization of society in which production is managed by private initiative with view to private profit. Needless to say, on the one hand, that this implies nothing about the social results of such an organization and, on the other hand, that alternatives to it are many and not satisfactorily

covered by the single word "socialism".

II. We must beware of the error implied in the widespread belief that it is economic performance which decides the ultimate fate of any form of social life. Not only are people perfectly unable to form an unbiased judgment about alternative possibilities (they would be unable to do so even if alternatives ever stood actually working before their eyes under exactly the same conditions) but mere economic performance would not in any case be decisive by itself. We observe, it is true, that advocates of either capitalism or socialism invariably hold that the system they espouse offers or would offer to the masses a higher standard of life than its competitor. This misconceives the real issue. More important than standards of living are the types of people and the civilization which a given system turns out; more important also for everyone of us is the question whether a given system agrees with our moral values and our cultural volition. But what people think and want is a secondary matter anyhow. The important thing is the logic of social situations, which among other things, makes people think and feel as they do.

If nevertheless we ask the question of performance, that is to say, the question what economic results may reasonably be expected from the mere working of the capitalist machine in the decades before us, it is only because for the economist that is the relevant question and not because we believe that the issue will be decided on this ground. In order to answer it we make the following assumptions: First, we assume that there is a precise meaning to the concept of total output of commodities and services. This is really the boldest assumption of all. It implies begging a fundamental problem of modern theory, but the reader is so accustomed to using that concept as if it were entirely unproblematic that he is not likely to have any qualms about it. Secondly, we assume that the function descriptive of the distribution of money incomes according to amount remains invariant. If this were an assumption about the actual course things may be expected to take it would almost certainly be contrary to fact. What we mean is that if the working of the capitalist machine were not interfered with that distribution would remain as it is. The warrant for that is in the fact that for the last hundred years that distribution has remained, as far as our statistics allow us to form an opinion, substantially invariant over time, although it fluctuated within the cycle. It is not necessary to assume the form suggested by "Pareto's Law", although ~~the speaker~~ thinks that critics have been somewhat unjust to that piece of analysis. But whatever the form of the function is, invariance is necessary for our argument, both because only if distribution in that sense is invariant can we conclude that variations in average income are by themselves sufficient to describe how all classes of society are going to be affected by a given increase in total output and because capitalist economy could not continue to work on at this same rate of progress if that distribution were so substantially changed as to interfere with the accumulation from the larger incomes, which is an essential piece of the capitalist mechanism and largely accounts for such efficiency as it has. Thirdly, we assume the absence of such events as world wars and revolutions.

Now, average income per head was about $700 a year in 1928. It is a conservative estimate that total physical output increased on the average at 3% compound interest per year practically as far back as our data carry us. Most readers

will be familiar with the more important of the indices which have been constructed to show this, and most of which would, indeed, support a more optimistic estimate, such as the indices of Warren and Pearson, Snyder, Day-Thomas, the Federal Reserve Board, the Department of Agriculture and others. Extrapolating and retaining the purchasing power of the monetary unit at the level of 1928, we get about four times (4.38) as much for 1978. This must be corrected for increase in population, which is an exceedingly controversial matter. Accepting Mr. Sloane's estimate of about 160,000,000 for that year, we come to the conclusion that an average income of about $2100 per head of population, purchasing power of 1978, would be reached about that time. Such performance may be considered satisfactory or unsatisfactory - that is a matter of taste and will largely depend on one's extra-scientific predilections. It certainly allows of the formulation, if we assume relative shares to be unchanged, that anything which according to our present ideas we should call poverty, would be done away with, even in the lowest strata of society, defectives alone excepted.

III. It goes without saying that injuries may be inflicted and even expected to be inflicted on the organism which will prevent it from producing the result glanced at. This is all the more serious a qualification because many things perfectly unavoidable under present ideas and standards, come within the meaning of those injuries. Very sharply progressive taxation alone would be sufficient. And so would be attempts to soften the hardships of adaptation to new situations as they arise in the course of industrial innovation. However, such injuries have never been absent and our 3 percent leaves plenty of latitude for the absorption of the effects. For this country that figure includes even the wastage of the world war. The rate would be different, of course, for European countries. It should be observed that when we speak of "injuries" we do not necessarily imply an adverse judgment. What is an injury within our strictly technical meaning may be an improvement from many other standpoints.

But the fundamental question is whether we are justified at all, injuries or no injuries, in looking upon persistence of that rate as at all likely. A majority of students of the phenomena of economic development (we had better avoid the word "progress") is inclined to doubt it, and you know that many authors, among whom we may mention S. Kuznets and A. F. Burns, have even tried to establish statistically the presence of systematic retardation. We need not repeat the familiar arguments which may be leveled against their methods but can confine ourselves to adding one more: material at all adequate to the task of forming an idea about the behavior of total output over time does not go back beyond 1870. If, in order to avoid the troubled time of the World War, we stop in 1913, that material covers two branches of what the speaker is in the habit of calling the Kondratieff wave. Quantitative study of economic cycles was, as you know, initiated by Clement Juglar. He assumed, as many students still assume, that there was just one such wavelike movement. But there are, on the one hand, theoretical reasons to expect that there should be many waves of different period rolling along together and superimposing themselves on each other, and there is the statistical fact that a "many cycle hypothesis" fits our time series much better than a "single cycle hypothesis". Mr. Kitchin and Professor Crum have established, as the speaker thinks beyond doubt, the existence of what is usually called the forty month

cycle, and Kondratieff discovered and described a very much longer wave which ~~the speaker~~ thinks has an average period of about fifty-seven years. For reasons which it is impossible to enter into here, the rate of increase of total output is greater in the downgrade than in the upgrade of the long swing - which is just the opposite of traditional opinion and should by the way lead us to revise the traditional judgment about the relative merits of "prosperity" and "depression". Now 1870-1897 lies on the downgrade of a Kondratieff cycle and 1897-1913 just covers the prosperity phase of another Kondratieff cycle. On the theory alluded to we should therefore expect that in the first span increase of total output was at a greater rate than in the second span. If this be so it would follow that our material would have to display what looks like retardation but should not be taken as an indication of a long time trend.

However, it is urged sometimes that the prewar rate of increase was due to the opening up of new countries both as sources of supply of raw materials and as markets for industrial products and must therefore be considered as historically unique. There seems to be a mistake in this, which may be linked to a particular interpretation of the old law of diminishing returns. What the theorem thus designated really says is merely that if you add successive increments of one factor of production while keeping constant both the quantities of the other factors and the method of production, you will get, from a certain point onwards, decreasing increments of product. If we designate by P physical product and by V_1, V_2 .....V_n factors of production, then the partial derivative $\frac{\partial P}{\partial V_i}$, is in the useful interval a decreasing function of V_i. But what the theorem was made to say was that however you change methods of production and however you combine, or add to, factors, nature will in the end display a decreasing response to your efforts. There is no warrant whatever for this. Of course, new countries counted for very much in the developments of the nineteenth century and ~~even of later times~~, but the process of opening up new markets by means of developing new countries is only one member of a very large family which we call innovation. The introduction of new methods of agricultural technique for instance may shift the production just as, and more effectively than, taking new countries under the plow and achievement in that line is perfectly unpredictable. Once we have surveyed a given agricultural area, then given certain methods of production, it is easy to arrange, with reference to that method of production, all the plots of land existing in that area into a descending order of fertility or locational advantage, and to say that we shall take into cultivation first the "best" plot and then successively the worse ones, but we cannot say the same thing about the world of technical innovation which is not known to us and essentially refractory to survey. Hence there would be no sense in holding that we have been developing the most productive innovation so far and that only less productive ones are left for the future. This may be so, but the contrary is just as likely. In fact there is a reason to assume that the rate of technical progress will quicken rather than slacken. A hundred years ago, and still more so in the more remote past, innovation was a matter of individual will and vision, carried into effect

in the teeth of strong opposition. Now it is becoming increasingly mechanized so that organized research might be expected to turn out new methods which then will automatically be put into practice, much more systematically in future than has been possible in the past. Hence nothing is to be feared from either the law of diminishing returns or any of the arguments usually associated with it, as contemporaneous experience amply shows; lack of raw materials is not exactly what we suffer from.

IV. This is not to say of course that there are not other elements in the social situation of our time which may be very effective in producing retardation. They are of a socio-psychological kind. To begin with, every social or biological group applies itself to the task which is socially most important from the standpoint of the survival-interest of the group as a whole. This proposition is essential for what is to follow and should be carefully pondered and verified. Equally essential is the corollary that the social function which at any given time is the most "important" one in that sense, and success in filling it, supply the fundamental explanation for the emergence and the passing of what we call a Ruling Class. For instance, in a primitive agricultural tribe which has no means of defending itself by physical force and which is given to magical beliefs, say, of the animistic kind, magicians will be looked upon as the persons most important to the tribe and hence will rise into positions of social prominence and form, if the social environment is stable enough to allow of differentiation of a hereditary sort, the upper or ruling class of the community. Again, in conditions in which warfare and readiness for warfare are necessities of daily life and in which the technique of warfare is such as to require lifelong training (Such as the medieval technique of managing sword and lance on the iron clad horse), a class of warriors will grow up, establish itself as the socially ruling stratum and impress on the social body its own scheme of values and the form of life dictated by its interest and visions. Similarly, at a later stage and for reasons we cannot enter upon here, the function of economic leadership became in most countries we should be inclined to call "civilized", the socially most important one. To be sure, it was not economic leadership in general but an economic leadership moulded by preceding conditions and by the necessities of the historical environment - that kind of economic leadership which took the form of individual enterprise. And from these social necessities, and by filling that entrepreneurial function, the bourgeois class climbed into the saddle, impressing in turn its own values, interests and standards on the social psyche. We shall return in a moment to carry on this argument. Just now it is sufficient to point out that the very success of bourgeois capitalism tends to reduce its own importance for the future. As a result of its achievement that fear is rapidly dropping away from humanity which trembles in the prayer, "Give us this day our daily bread". As soon as this is the case, economic affairs will cease to hold that central position in the feeling and thinking of mankind that they used to hold and energies will not so exclusively be concentrated on economic tasks. This might well account for a considerable amount of retardation in the future.

Moreover, the success of capitalism, such as it is, is closely linked up with the method of selection for leading positions which was characteristic of a substantially

competitive system. It is worthwhile emphasizing that of all methods of selecting leaders which the speaker either historically knows or can think of, that is the only one that effectively tests the qualities which make for success once the leading position is conquered. The qualities that make a good candidate for political office are entirely different from the qualities that make a good administrator of the same office. But the qualities that make a man rise in competitive business are precisely the qualities which will make him a success when he has risen. It should also be observed that this important characteristic is rapidly vanishing from the world of giant concerns. But as the success of capitalism is fundamentally linked up with a peculiarly effective type of responsibility which consists in having to pay for one's mistakes: A politician who can make a successful speech or a public servant who can write a successful report, need not worry about an unsuccessful measure. But no ability of speaking or writing will be of any help to an entrepreneur if the balance sheet looks wrong. This again has ceased to be so in a rapidly expanding sphere of modern business. Finally, past success of the capitalist system rested largely, whatever some of the speaker's fellow economists may say, on that peculiar kind of financing enterprise which presupposes considerable inequality of income. It is not necessary to quote any statistics in order to convince you that the percentage of saving increases with the size of incomes. It would be necessary, however, to show that and why that method is so vital. But this we cannot do here. The disapproval of inequality and consequent attack on it is, however, an essential feature of modern political psychology and must be expected to asser itself more and more. Retardation from all those causes is, of course, more than likely and that is why we were so anxious to make above that qualification about "injuries" to the organism.

V. What has just been said by way of commenting upon and qualifying the expectation which might be formed about capitalist performance in the future from its performance in the past, immediately leads us back to the question at the head of this paper.

On the one hand, if capitalism is doomed it is certainly not doomed because of any rational proof that its economic performance is unsatisfactory in the sense that a country such as this could be reasonably expected to do better with respect to increase of total output by any of those alternatives which are at all within range of practical possibility. No doubt much more of fact or argument would be necessary to establish this proposition. We cannot do more than add a few remarks. To begin with, it must be borne in mind that much less weight than appears at first sight attaches to the argument which is resorted to by most of those people who otherwise and as a matter of trend would profess themselves quite satisfied with the rate of increase we actually observe, viz. the argument from fluctuations and the losses and sufferings incident to recurrent crises. If, following usage, we primarily stress the element of unemployment it must not be forgotten, first, that as a matter of arithmetic, the capitalist organism is at present, and can be expected to be still more so in the future, perfectly able to take care of the unemployed members of society. To put their services to some use and to prevent them from going to waste is of course one of the most obvious tasks of rational Planning. But whether or not this problem be successfully solved, the fact remains that the working of the

capitalist machine supplies all the means necessary to avoid anything that any people have a right to call suffering who speak quite coolly of such events as the "liquidation of the Kulaks." Secondly, it is matter of historical fact that those sequences of events which we identify as great crises or catastrophes can in no single instance be explained by the working of capitalist business alone. There are always, precisely in the worst cases, "external factors" present, wars, mistaken policies and so on. This field is, it is true, so much infested by monomaniacs especially of the monetary type that that should be obvious common sense is by no means easy to establish. But to any unprejudiced person it should be clear that the working of a system (never mind what system; think, for instance, of a system of balls connected by elastic strings) is one thing and interference with the system by external factors is another thing. This is no argument for laissez faire. On the contrary it is an argument for regulation that rests on an understanding of the material of the capitalist machine. But it is still very relevant to a judgment about the results attributable to that machine.

Furthermore the argument that private industry and trade work with an undue amount of wastage of resources, while possibly quite true, can not be made out by simply listing all cases in which a given result could have been achieved by smaller expenditure in terms of real resources. The usual method implies a comparison between the actual working of one system with the ideal of another, and entirely neglects the sources of waste which we might expect to discover were that other system put into practice. Apart from this many of the examples usually adduced are unconvincing because they often mean no more than that experimenting with new things frequently leads to failure. Such failures may be unavoidable in any system and what looks like unqualified failure may have its function all the same. Even what looks like simple social waste sometimes has a function. There is, for instance, certainly a great number of people engaged in running inefficient small retail shops, but the presence of those retail shops takes care of many people who would otherwise be temporarily destitute in the course of adaptation of rapid technological change. Now this may be an uneconomic way of taking care of them but the point is that we must not look upon the phenomenon as if it were a mere blemish and nothing else. Careful analysis on such lines reduces very much the strength of the prima facie case.

Again the argument from over-capacity, over-investment and over-production loses much of the weight it seems to carry the moment we realize that the more successfully progressive an economic system is, the greater will be, at any point of time, that amount of capacity which has been set up with a view to future demands and that amount of capacity which is already semi-obsolete. It is impossible to tell what would be left after deduction of those two items to which moreover it would be necessary to add all the capacity produced in order to cope with cyclical peak demand. Similar considerations apply to the case of over-production as distinguished from over-capacity apart from the fact that, taken in the ordinary sense, general over-production has no meaning at all.

These examples must suffice, but however we may think about them and other equally familar ones, so much is certainly true that the case against the performance of the capitalist system is much less strong and much less clear than public opinion seems at present to assume. Whatever the result of striking a

balance might be, had we the time to undertake the task, it is practically certain that it would not be spectacular and that it would not consist of negative items alone. In particular there is no excuse for holding either that if capitalism be left to itself things would, particularly for the masses, go from bad to worse or that the capitalist system displays any inherent tendencies towards economic breakdown. Both propositions have, as you know, been held by Karl Marx. But both have been given up by the leaders of Neo-Marxism. This is not astonishing with respect to the first, for it would indeed be difficult to hold that the capitalist machine turns out a standard of life for the masses that decreases over time. So after efforts had been made to interpret Marx, in the face of obvious evidence to the contrary, to have meant not absolute real wages, both totals and rates, but the relative share of the working class (in which sense he would also be wrong of course), that proposition was silently dropped. It is much more remarkable however that the Neo Marxists, from Hilferding onwards, also dropped the other, for owing to the recurrent hysterics about crises it would not have been tactically impossible for them to uphold it. But they were much too good economists to do that and hence handed the thing over to the literature of popular Marxism in which it flourishes still. It would follow, although this was, as far as the speaker knows, too much for them to admit explicitly, that it is no longer possible to base the case for socialism on the claim that in abolishing poverty it would do what the rival system was intrinsically incapable of achieving.

But, as pointed out before, this is not all nor even the decisive point. We might be socialists even if we recognize superiority of capitalism as an economic machine. There are higher things involved in one's social ideals than beefsteaks and movies, and even if it were not so, the future course of things would depend on the economic working and results of the capitalist system in a different and less direct way than that which lies between economic performance and rational choice of people. We may conveniently divide our argument into a psychological and a sociological branch, although there is of course no sharp dividing line between them. Every economic system moulds the souls of men by determining their working day and, through it, the attitudes, ideals and habits they develop. Capitalism rationalizes human thinking and human behavior. Examples to show that could be adduced in plenty from double entry bookkeeping to Neo-Malthusianism. This will produce concentration on the individual's interests and particularly interests amenable to rational formulation. All in human life that cannot stand the test of a very superficial kind of rationality is likely to be discussed away. For our proposition it is primarily important to note two implications of this: On the one hand rationalization of economic activity means scientific method, first on the technical, then on the economic or business side and this again means the mechanization of progress previously adverted to. The modern entrepreneur compares to his predecessor of a hundred years ago very much as a modern general compares to that picturesque sort of individual that used to fill the same function a hundred years ago. Managing a modern army is now a mechanized job in which a great number of specialized workers cooperate to turn out the result ready made and thereby to reduce the commander-in-chief almost

to insignificance. The application is obvious. On the other hand, we see now much more clearly than previous generations have realized, who were content with very simple arguments and justifications, that most of the emotional values of life cannot be formulated in rational terms. Among them are some which are of the utmost importance to the capitalist class and to the motivation of its members. Although we could equally well exemplify by the changed relation between entrepreneurs and the physical set up of any given factory, we will merely touch upon the most important source of individual motivation in capitalist society, the family. Not only has capitalist evolution created a rationalized scheme of private life within which the family house and all that it stands for is no longer a necessary, or even convenient, form of life, but it has done away, or is about to do away, with all the motivation for economic action that center around it. This process has indeed gone to very different lengths in different countries and within the same country in different regions and social groups. Peasants and farmers are, so far, practically untouched by it everywhere, but it is superfluous to stay in order to show how completely it has changed the moral world of the upper Bourgeoisie. This being so, their grip loosens both on their former ideals and on the position which are valuable mainly because of those ideals. That is why there seems to be no "fight" in them, when the system which is theirs is being challenged, and why they do not seem to believe in it themselves. The speaker knows that this statement is contrary to widespread opinion. Most people would think that the Bourgeoisie is defending itself and its interests all right. But apart from the fact that this opinion often rests on nothing more than the naive belief of the intellectual in all sorts of mysterious powers behind the political scene, what is actually done by that class is as nothing compared with what it could do if the will to survive as a class were not dying out within it.

Sociologically it is clear that the prestige of the industrial and commercial Bourgeoisie with other classes never has been as great as the corresponding prestige of the warlike upper stratum in the middle ages. There are many reasons why achievement of the type that was open to those warriors, should have been particularly apt to impress the masses that served them. No businessman, however successful in his office can ever hope to look to the rest of his countrymen as the knight did on his horse and in his armor. The latter's social function also carried the particular advantage that it lent itself as no other social function ever did to the direct and physical defence of the interests of its incumbents. To be able to draw one's sword in order to deal with an opposition necessarily deficient in the only technique available, is much more effective than to have to lobby with politicians or try to acquire control of newspapers and the like. It is indeed only with serious qualification that the Bourgeoisie could ever have been called the ruling class at all. In Europe it practically always submitted to the remaining feudal elements which in exchange protected it and drew a new lease of life from the fact. The great exception afforded by this country is accounted for by the absorbing fascination of developing an environment of great possibilities, and should not be relied on for prognosis as to the future. It is by no means astonishing that his origin, his past history and his

kind of work and mode of life should make the Bourgeois an ineffective leader or ruler. It would be astonishing if it were different. Hence social critique turned against him very much more promptly than it did against the feudal powers. The ideas of political democracy which he had made his own in the time of his servitude proved incompatible with the essentially monarchical ideas underlying the organization of business, all the more so because his democracy was typically of the eighteenth century type, and tinged with equalitarian elements which he soon learned to disapprove but which he never could successfully get rid of. The very increase in the standard of life, self-confidence and leisure in the masses which may be attributed to the working of the bourgeois economic system, produced an opposition which checkmated its upper stratum politically as soon as its feudal protector fell.

There is no need to elaborate this argument; it is clear enough in what sense it supplies a negative answer to our question. The interesting point about it is that, as far as ultimate results go, our answer is the same as that which socialists would give. Besides, there is the further affinity that we also link a prognosis unfavorable to the capitalist system to its economic results. But it is not its economic shortcomings that threatens it. On the contrary it is its economic achievements, and their effects on the human psyche and on the social and political structure of society, that is likely to kill it eventually.

It is another question how this prognosis may be expected to materialize. Some people like to indulge in speculation about the likelihood of revolutions. All we can say about that is this: What we term a revolution is akin to what in economic life we designate as a crisis or panic. Now an economic crisis is not the essential thing about economic evolution or, for that matter, the economic cycle. Fundamentally that wavelike movement that pervades economic life could go along and remain what it is, without those breakdowns for which we reserve the term crisis. The sum of phenomena we usually designate by it owes its existence to accidental circumstances. It may or may not occur and sometimes occurs on less provocation than there is in cases in which it is avoided. But in certain phases of the cycle those accidents are very likely to occur. Similarly what we call a revolution is nothing but a collapse of organization and morale. Whether it occurs or not is, from a long time view, of secondary importance and depends on random combinations of circumstances. This implies that our views about the likelihood of such events should differ for different countries, races and historical junctures. It is more important to note that, even apart from this, the outcome glanced at above though following logically from observable fact is by no means a certainty. Before humanity chokes in the dungeon of socialism it may well burn up in the flames of nationalist wars. The normal expectation for the Anglo-American world, however, is on the lines of a steady bureaucratization of economic life as well as of much besides.

Suggestions for the Quantitative Study of the Business Cycle.

2

Suggestions for the Quantitative Study of the Business Cycle.+)

Three lectures (~~with discussion~~ each to be followed by a discussion)

by Joseph A. Schumpeter

I.

Clearing the Ground (cp. Tinbergen's Survey I and II)

(1) ~~When~~ we say that "cycles" are present in economic time series we merely mean the facts a) that time series ~~are~~ or their time-derivatives are never monotonic b.) that their "fluctuations" are related to each other. There is no reason to assume that the cycles in this sense are all of one kind, nor that ~~such kind of fluctuations given rise~~ cycles of any given kind should ~~be periodic~~ display constant periods. In those cases however in which the periodogram analysis has been successful (Cram, Greenstein) actual fluctuations must fairly correlate with a pure sine curve. Prima facie evidence justifies the expectation that ~~cycles~~ must

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causes, ~~gives~~ rise to several "fluctuations" or "vibrations".

~~(2.) Cycles may arise from non-cyclical causes, cycles which perturb the whole mechanic system from technical causes.~~

The ~~[illegible]~~ (time-lapse) of a factor which produces cycles need not ~~itself~~ (be) ~~display cycles~~ cyclical itself. ~~A~~ Such a factor may be an "impulse", or simply a property of the system. If it is an impulse of the non-cyclical kind, (then) the cycles are the form in which the system responds to disturbance and the analogy with a resonator suggests itself ("waves of adaptation".) The most familiar example is afforded by the "animal cycles" (hogs, sheep, cattle). Unless we exclude all impulses from our variables and ~~exclude~~ include them among data, our system is not "causal" in the sense of Birkhoff and Lewis, that is to say it is not possible to describe its evolution in time (uniquely) in terms of initial conditions. Even ~~if~~ so far as this is possible the system may not have any static solutions. The value of the concept of equilibrium as a tool of business cycle analysis is however not much impaired by this possibility.

~~& the factor which produces cycles in all the variables of the system need not of course~~

3

(3) Cycles in the system as a whole (general cycles) can of course arise from particular causes, such as harvests. The variable that sets into motion a general cycle in social aggregates (total deposits, total output, price level and so on) need not itself be an aggregate. Even if it is (alteration of gold content of the dollar, for instance, involve a change in an aggregate) it practically never directly acts on other aggregates but only through, say, prices and quantities of individual commodities. Hence statements about relations in time between aggregative quantities ("macrodynamic theories") never go beyond the surface and are likely to be either empty or misleading as regards prognosis and as regards diagnosis. The quantitative study should be, much more than it actually is, be directed towards the details of the industrial processes that lie behind those aggregates.

4

II.

Facts, Schemata, Theories (cp. Tinbergens Survey III, IV, V)

(1.) Most of the facts we agree on are facts of aggregative behavior (see I 3). ~~Hardly any~~ Difference of opinion arises, however ~~even within some~~ as soon as these facts are being treated ~~and~~ even expressed. The outstanding example of the former type of difference is trend analysis. The outstanding example of the latter type is the manner in which different ~~authors~~ investigators deal with exceptions. Nothing is more plausible for instance that general unemployment percentage invested should vary with the rate of change of price level. In England, 1871–1914, it does so in 22 instances and fails to do so in ~~1~~ 16. The question what such a finding means immediately leads into "theory."

(2.) There are a number of schemata which ~~[illegible]~~ aim at describing pieces of the cyclical mechanism, ~~[illegible]~~ such as ~~the~~ lagged ~~mistakes in business~~ ~~adaptation~~ reaction or ~~adaptation~~ reaction in function of the ~~rates of change of a quantity~~ rate of change of another variable ~~in the~~ variable and so on. If it is in the working out of such schemata that mathematics has so far rendered the most conspicuous service to business cycle analysis. We may distinguish particular and general schemata and exemplify

(2.) Schemata are descriptions of certain pieces of the cyclical mechanism, in the most ambitious instances they ~~and~~ claim to depict the whole of it. One class may be exemplified by the schemata of lagged adaptations (mentioned in I 2) or of reaction depending not only on the values of some independent variables but also its first-derivatives. Another class is represented by a development which flows from the old quantity theory of money which can easily be "dynamized" in such a way as to issue into the Keynes-Amoroso-Vinci equations (see the latter's article in Econometrica Vol II no 2).

These schemata are purely formal and compatible with almost any views about the nature and cause of business cycles. But their authors often add an interpretation which goes beyond ~~that~~ ~~and~~ ~~can~~ those mechanisms and then ~~fall into the~~ are liable to believe that statistical facts which verify the schema also verify that interpretation. To clear up this matter it will be useful to analyze the Kalecki schema and to ask what it ~~you~~ really asserts about the cyclical process.

Suggestions for the Quantitative Study of the Business Cycle.

Three Lectures (each to be followed by

6

(3) Interpretations of mechanisms or causes we call Theories. They can be grouped under the headings: External-Factor-Theories, Monetary Theories, Others. Since any analysis must take account of all the facts that [illegible] to which the various theories appeal, common ground should extend very far. If it does not this can be due only

a) to unwarranted assertions about fact. For instance, the speaker believes that the current views about the effects of saving are not only wrong in logic but also in fact since they imply gross overstatement of the actual yearly amount of saving.

b.) to faulty argument. A theory may be right in all the assertions it makes about the facts from which it starts and yet fail to establish the desired conclusion. The oversaving-theories again afford an instance.

c.) to difference in emphasis and (particularly in evaluation) of causal significance. The "Hayek-effect" for instance is very real. Its presence can be well established historically. Yet it fails as a theory of the cycle. [illegible] behavior of the elements it traces has [illegible] relative

Three Lectures (each to be followed by a discussion)

7

III.

Questions of forecasting and policy. (cp. Harvard Survey VI.)

Although neither forecasts nor policies are among the primary objects of these lectures, questions relating to both may serve to clarify and develop a few additional points.

(1). Forecasting from a series of states of the economic organism and forecasting what will actually happen, are of course entirely different things. So are forecasts about future events as such and forecasts about the precise timing of these events. Forecasts of the former type are possible and interesting although of very limited value to the businessman or at that time speculator. ~~to the speculator the forecasting value of the element~~

(2.) The first question as to policy which business cycle analysis can be expected to answer is what sense there is in ~~fighting~~ trying to counteract cyclical variations at all. Agreement can be hope for only with respect to certain features or phases of these variations, beyond which difference of opinion is likely to persist.

But another group of questions is more hopeful: ~~if~~ we can strictly remain in the realm of ~~effects~~ scientific reasoning if we confine ourselves to an investigation of the effects to be expected from any given policy. ~~Examine of a simple case~~ ~~Our discussion~~ As an example the influence of various cyclical interventions of various age policies will be discussed.

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(2) The time-shape of a factor which produces cycles need not be cyclical itself. Such a factor may be an "impulse", or simply a property of the system. If it is an impulse of the non-cyclical kind, then the cycles are the form in which the system responds to disturbance, and the analogy with a resonator suggests itself ("waves of adaptation"). The most familiar example is afforded by the "animal cycles" (hogs, sheep, cattle). Unless we exclude all impulses from our variables and include them among data, our system is not "causal" in the sense of Birkhoff and

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Lewis, that is to say, it is not possible to describe its evolution in time uniquely in terms of initial conditions. Even so far as this is possible the system may not have any static solutions. The value of the concept of equilibrium as a tool of business cycle analysis is however not much impaired by this possibility.

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to certain features or phases of those variations, beyond which difference of opinion is likely to persist.

But another group of questions is more hopeful: we can strictly remain in the realm of scientific reasoning if we confine ourselves to an investigation of the effects to be expected from any given policy. As an example the influence on cyclical situations of various wage policies will be discussed.

"Suggestions for the Quantitative Study of the Business Cycle"

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1. This title is the same as that chosen by Professor Tinbergen for his excellent survey in Econometrica Vol. 3, July 1935. It has been thought convenient to arrange topics in the order in which they are dealt with by Tinbergen, and to start from Tinbergen's treatment. This time-saving device will, however, work only if participants familiarize themselves beforehand with the content of that survey. Also they should bring their copies. A limited number of copies will be available for $1.00, or for loan.

Lewis, that is to say, it is not possible to describe its evolution in time uniquely in terms of initial conditions. Even so far as this is possible the system may not have any static solutions. The value of the concept of equilibrium as a tool of business cycle analysis is however not much impaired by this possibility.

(3) Cycles in the system as a whole (general cycles) can, of course, arise from particular causes, such as harvests. The variable that sets into motion a general cycle in social aggregates (total deposits, total output, price level and so on) need not itself be an aggregate. Even if it is (alteration of gold content of the dollar would, for instance, involve a change in an aggregate) it practically never directly acts on other aggregates, but only through, say, prices and quantities of individual commodities. Hence statements about relations in time between aggregative quantities ("macrodynamic theories") never go beyond the surface and are likely to be either empty as regards diagnosis ~~and~~ or misleading as regards prognosis. Quantitative study should be, much more than it actually is, be directed towards the details of the industrial processes that lie behind those aggregates.

II.

<u>Facts, Schemata, Theories</u> (Compare Tinbergen's Survey III, IV, V)

(1) Most of the facts we agree on are facts of aggregative behavior (see I.3). Difference of opinion arises, however, as soon as these facts are being treated or even expressed. The outstanding example of the former type of difference is trend analysis. The outstanding example of the latter type is the manner in which different investigators deal with ex-

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ceptions. Nothing is more plausible, for instance, than that general unemployment percentage inverted should vary with the rate of change of price level. In England, 1871-1914, it does so in 22 instances and fails to do so in 16. The question what such a finding means immediately leads into "theory".

(2) Schemata are descriptions of certain pieces of the cyclical mechanism; in the most ambitious instances they claim to depict the whole of it. One class may be exemplified by the schemata of lagged adaptation (mentioned in I 2) or of reaction depending not only on the values of some independent variables but also ~~its~~ on their time-derivatives. Another class is represented by a development which flows from the old quantity theory of money which can easily be "dynamized" in such a way as to issue into the Keynes-Amoroso-Vinci equations (see the latter's article in Econometrica Vol II no.2).

These schemata are purely formal and compatible with almost any views about the nature and causes of business cycles. But their authors often add an interpretation which goes beyond those mechanisms and then are likely to believe that statistical facts which verify the schema also verify that interpretation. To clear up this matter it will be useful to analyze the Kalecki schema and to ask what it really asserts about the cyclical process.

(3) Interpretations of mechanisms or <u>causes</u> we call Theories. They can be grouped under the headings: External-Factor-Theories, Monetary Theories, Others. Since any analysis must take account of all the facts to which the various theories appeal, common ground should extend very far.

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If it does not, this can be due only

(a) to unwarranted assertions about fact. For instance, the speaker believes that the current views about the effects of saving are not only wrong in logic but also in fact, since they imply gross overstatement of the actual yearly amount of saving.

(b) to faulty argument. A theory may be right in all the assertions it makes about the facts from which it starts and yet fail to establish the desired conclusion. ~~The~~ Some oversaving-theories again afford an instance.

(c) to difference in emphasis and particularly in evaluation of causal significance. The "Hayek-effect" for instance is very real. Its presence can be well established historically. Yet it fails as a theory of the cycle.

III

Questions of forecasting and policy. (Compare Tinbergen's Survey VI.)

Although neither forecasts nor policies are among the primary objects of these lectures, questions relating to both may serve to clarify and develop a few additional points.

(1) Forecasting from a series of states of the economic organism and forecasting what will actually happen, are of course entirely different things. So are forecasts about future events as such and forecasts about the exact timing of these events. Forecasts of the former type are possible and interesting, although of very limited value to the businessman or short time speculator.

(2) The first question as to policy which business cycle analysis can be expected to answer is what sense there is in trying to counteract cyclical variations at all. Agreement can be hoped for only with respect

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to certain features or phases of those variations, beyond which difference of opinion is likely to persist.

But another group of questions is more hopeful: we can strictly remain in the realm of scientific reasoning if we confine ourselves to an investigation of the effects to be expected from any given policy. As an example the influence on cyclical situations of various wage policies will be discussed.

Suggestions for the Preliminary Study of the Business Cycle

CAPITALISM IN THE POSTWAR WORLD

by

Joseph A. Schumpeter

I

For the purposes of this essay capitalism will be defined by three features of industrial society: private ownership of the physical means of production; private profits and private responsibility for losses; and the creation of means of payments - banknotes or deposits - by private banks. The first two features suffice to define private enterprise. But no concept of capitalism can be satisfactory without including the set of typically capitalistic phenomena covered by the third. Where it is absent we might speak of commercial society. By socialism we shall mean an institutional arrangement that vests the management of the productive process with some public authority.*

In trying to forecast the role, if any, that capitalism in the sense defined may be expected to play in the postwar world it is well to remember that its fate is not a question of the merits or demerits we

* It should be noted that this definition of socialism is not only purely economic but also purely formal. It says nothing about the structure and character of a socialist society, e. g., whether it is equalitarian or not, warlike or pacific, democratic or authoritarian. Friends and foes of socialism are in the habit of endowing their concept of it with additional traits and hence in general mean by it something much more specific.

may individually see in it. Our judgment about these is a matter of personal or group-wise preference that depends on interests and ideals largely determined by our personal or group-wise location in the social organism. What we really mean when we say that we are for or against capitalism, is that we like or dislike a certain civilization or scheme of life, which is historically associated with the three economic features mentioned. But civilizations are incommensurable. Even if we agreed to neglect those cultural aspects which are what really matters to us, and to make the "desirability" of retaining or eliminating capitalism turn on some purely economic criterion - such as comparative productive efficiency - we should never agree about the result. For even if those extra-economic and largely extra-rational preferences did not prevent us from admitting that any criterion could ever tell against the alternative we have chosen to espouse - which they no doubt would in most cases - we should immediately challenge a criterion that did. No amount of honest intention to place oneself on the standpoint of the public welfare or of the nation's interest would avail against that. For the point is precisely that these words mean different things to different minds. The only thing we can do in something like a scientific frame of mind is therefore to try to visualize, irrespective of our wishes, the actual situations which may be expected to emerge and the relative power of the group which will be in a position to assert their interests and ideals in handling those situations.

Another point should be borne in mind. No social system is ever pure either in its economic or in its political aspects. As regards the former, structural principles, such as, in the case of commercial society,

private management of the process of production and free contracting, are never fully carried to their logical consequences. People were at no time allowed to do with their own quite as they pleased, and society at all times limited the range within which they might freely contract. In the epoch of intact capitalism law, custom, public opinion, and public administration enforced a certain amount of public planning, while in a society that had adopted the structural principles of socialism there was such a thing as Lenin's New Economic Policy that left room for a certain amount of laissez faire. It follows that, public management or planning being never either absent or complete, our question concerning the immediate future should not be couched in terms of "capitalism or socialism": there is a great variety of intermediate possibilities.

Still more important for social diagnosis and prognosis is, as we shall presently see, the fact that no society is ever homogeneous. By this I do not merely mean that the political sector of every society grows out of, and hence reflects, all the different interests and attitudes of the various groups and classes that the prevailing social system produces. I mean something much more fundamental: every society contains, at any given time, elements that are the products of different social systems. Thus, feudal society harbored, besides the lords and peasants and artisans that constituted the essential elements of its system, also other elements - traders, for instance, and certain classes of producers - that did not belong to the feudal organism and dwelt in towns which that organism failed to subjugate or to assimilate. In the capitalist epoch, the classes that are the products of the capitalist process are hardly ever found alone. Practically always they exist in symbiosis with an aristocracy and a

peasantry of non-capitalist origin. And this fact is not only, as one might think, responsible for frictions and other secondary phenomena. It is of the essence of the social process. A purely capitalist society - consisting of nothing but entrepreneurs, capitalists and proletarian workmen - would work in ways completely different from those we observe historically, if indeed it could exist at all.*

II

Both in its international and in its domestic aspects, capitalist economy is adapted to the requirements and habits of a normally pacific world. "Total War" under modern conditions calls for a concentration of effort much more stringent than the mechanism of capitalist markets can achieve. War-time planning by government in fact suspends the normal operation of capitalist processes. In doing so it develops, on the one hand, economic structures and situations and, on the other hand, new social organs and positions of power which do not automatically disappear with the emergency that brought them into existence. They have to be liquidated, if at all, by a series of distinct measures which naturally meet resistance. We have seen that the outcome of the ensuing struggle will not depend on any abstract desirability of a return to prewar ways but on the political forces marshaled for and against it.

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* Many readers will feel that while this might apply to European and Asiatic countries, it could not possibly apply to the United States. But it would be easy to enumerate the very particular conditions - now rapidly passing - which explain why a purely bourgeois regime was in this case able to hold its own for so considerable a time.

The strength of these forces in turn will depend, first, on the duration of the war in question and, second, on the vitality of the capitalist system independently of the war. Thus, in 1919, the United States emerged from a spell of war-time planning that had been both mild and short. The various war boards and their bureaucracies had not had time to get into full working order, let alone to settle into positions which they would have looked upon as permanent. The business world and the public in general had not had the time to get accustomed to their rule and to accept them as part of the normal scheme of things. Moreover, all the groups that counted politically were fully determined to stand for private enterprise and in fact did not clearly perceive an alternative - which fact indicates precisely that the vitality of American capitalist society then was not yet substantially impaired.

This historical instance should not blind us to the possibility that events such as total war may influence social evolution more profoundly than words like "catastrophe" and "conflagration" imply. They may create situations so compelling as to impose permanent departures from the lines previously followed, and attitudes greatly at variance with any observed before. They may change the distribution of political power in unpredictable ways. After all, the bolshevist regime is obviously of more than passing importance; yet it could never have established itself without the first world war and the largely accidental ways in which that war affected Russia. We may indeed succeed in interpreting the break as the result of existing tendencies that were merely accelerated by the war, and thus formally salvage historical determinism as a philosophy. But this does not increase its value as a working hypothesis.

There cannot be any doubt but that, in all countries concerned, the present war effort will put existing social structures under severe strain which may result in breakdown or fundamental transformation. The chances for this to happen are presumably greater in vanquished countries, but the victor countries are by no means exempt from this possibility. All the more important is it to raise the question of what we may term the tensile strength of the social systems that are being exposed to that strain.

It is a commonplace that capitalist society is, and for some time has been, in a state of decay. But there is no agreement about the precise nature of that decay. Differences of opinion on this point can be conveniently described in terms of two theories.

There is, first, the familiar theory of Vanishing Investment Opportunity.* It starts from an undeniable truth, more or less explicit recognition of which constitutes its chief merit. Unlike other economic systems, the capitalist system is geared to incessant economic change. Its very nature implies recurrent industrial revolutions which are the main sources of the profit and interest incomes of entrepreneurs and capitalists and supply the main opportunities for new investments - such as railroad building or the construction of electric power plants - and the main outlets for new savings. Whereas a stationary feudal economy would still be a feudal economy, and a stationary socialist economy would still be a socialist economy, stationary capitalism is a contradiction in terms.

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* The outstanding exponent of this theory is Professor Alvin C. Hansen; see, e. g., his Fiscal Policy and Business Cycles (1941), ch. I.

This becomes evident when we survey its most characteristic types, processes and institutions all of which would become atrophic in a stationary world.

Now the theory in question holds that this is happening in our day. That process of economic conquest is exhausting its possibilities. No very great innovations are in prospect and those minor ones that may be said to be in the offing, fail to stimulate entrepreneurship and investment either because they are capital saving rather than capital consuming or else because they are more suited to public than to private management. Moreover the great impetus given to investment in the nineteenth century by the opportunity of opening up new countries and sources of raw materials has spent itself. Finally the falling birth rate and the consequent slackening of the rate of increase in population tends to dry up a source of particularly calculable investments. For all these reasons the saving-investment process which is of obviously vital importance to capitalist society, works with increasing friction. Thrift, instead of being the means of expanding the industrial equipment becomes a cause of falling prices and of unemployment. Hence the necessity of injecting into an anemic system new purchasing power: the first and foremost application of this theory was in fact to provide a rationale for the fiscal policies of the past decade. Hence also - so we may continue for our purpose - progressive paralysis of the political organs of capitalist society and reduced ability to withstand shocks or to defend itself against attack.

This theory cannot be adequately discussed here.* It must suf-

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* I refer the reader to the discussion in my Business Cycles (1939), Vol. II, ch. XV.

fice to state that there does not seem to be any good reason for believing that, except as a temporary effect of the world crisis, the opportunity for great innovations in the economic process has been exhausted; that the tendency of innovations to become capital saving to the required extent has been illustrated by examples but has not been established convincingly; that the opening up of new countries, even if we assume it to be completed, was but one of many opportunities and might be replaced by others - in fact has been replaced by others during the twenties; that the falling birth rate, both through its direct effects on demand and through its indirect effects on motivation may become economically significant in the future but that it could hardly be used in an explanation of the course of events in the thirties even if the relation between the rate of increase in population and economic progress were less complex than it actually is.

The theory of vanishing investment opportunity obviously invokes the factors mentioned in order to deduce from them a state of perennial inadequacy of profit expectations or, to use Lord Keynes' term, of the marginal efficiency of capital. It is only by this effect on profit expectations that those factors can be held to account for insufficient investment and, in turn, for underemployment. But, surely, if profit expectations are the operative link in the deduction, it is natural to stress another element the reality of which cannot be called into question and which acted on profit expectations much more obviously, viz. the anti-capitalist policies adopted, in most European countries, ever since the first world war and in the United States, since 1933. The fact that both

in Europe and in the United States the capitalist process displayed unmistakable symptoms of strain exactly since the break in the legislative and administrative attitudes of public authority occurred may be significant. This element constitutes the pivot of the other theory.* It also starts from the proposition that capitalism is essentially a process of economic change and then goes on as follows.

One of the most familiar phenomena of that process of change, the full importance of which was first recognized by Karl Marx, is the emergence of large-scale business, which to some extent tends to compete out of existence - or, to use the Marxian phrase, to "expropriate" - small or even medium-sized firms. It stands to reason that, especially under conditions of democratic politics, this process weakens the political position of the industrial bourgeoisie, for a numerous stratum of businessmen owning and managing small or medium-sized firms is obviously much less exposed to political attack and in a much better position to withstand it than is a small number of salaried executives and large shareholders,** quite irrespective of comparative economic performance or "service." Moreover, within the big concern the pungent sense of property

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* I have developed it at length in my Capitalism, Socialism, and Democracy (1942), Part II.

** Here, any adequate exposition of that theory would have to digress into political sociology in order to show, that the behavior of a society toward a particular interest is primarily determined by the inducement and the opportunity for attacking it and only to a minor degree by what the observer according to his own standards may consider justifiable reasons for approving or disapproving of it. These reasons, so far as produced by political or intellectual agents, are simply rationalizations in the psychological sense.

and the will to fight for it tooth and nail withers away: the big concern thus not only "expropriates" some of its competitors but also its own capitalist interest. Those executives and shareholders are not only in a less favorable position to defend their ground than were the owner-managers of old but they meet attack in a much weaker spirit. Big business is in fact but a mid-way house on the road toward socialism.

The capitalist process undermines the structure of capitalist society in many other ways. I shall mention two only. First, it tends to destroy, economically or socially, the position of what may be termed the protective strata. The rise of the bourgeoisie ousted from political leadership the old aristocracies who knew so much better how to rule than does the businessman. The factory destroyed the old crafts and the department or chain store destroys the small trader who counted at the polls. It also reduced, relatively at least, the number of farmers and peasants. And so on. Second, capitalist civilization is a rationalist civilization. It tends to eliminate extra- or hyper-rational sanctions and habits of mind without which no society can exist.

Though the argument cannot be adequately developed, it should be clear that we have now before us the elements of a more realistic substitute for, or of a more realistic version of, the theory of vanishing investment opportunity and of the decay of capitalist society. The capitalist process itself produces, as effectively as it produces motor cars or refrigerators, a distribution of political power, an attitude of the public mind, and an orientation of the political sector that are at variance with its own law of life. It produces anti-capitalist policies,

i. e. policies that, regardless of individual intentions, interfere with its functioning according to its logic - the implications of which increasingly meet moral disapproval. Modern principles of taxation, although only one among many manifestations of the disintegration of capitalist society, afford perhaps the most telling illustration.

It is a nice question, on which it is much easier to differ than to agree, how far this decay has gone in any given case. Some symptoms showed in Europe before the first world war, but without it the majority of observers might have taken a long time in becoming aware of them. In the United States, the first unmistakable symptom of decay was perhaps the lack of spirit displayed by the bourgeoisie toward the end of the world crisis when the modal businessman proved that he was no longer up to tests imposed by his own order of things. That decay of capitalist society is very far advanced by now - everywhere - is not open to doubt. However much we may approve of some or all of the policies of the New Deal, we cannot fail to be struck by the absence of any serious resistance. A bourgeois society that meekly accepts the vast transfer of wealth accomplished in the United States during the thirties - I am not speaking of war taxation - thereby testifies to its readiness to surrender, though it may not be ready to surrender to every type of conqueror. It is in such conditions that events like world wars may acquire an importance in shaping the history of institutional patterns which they could never acquire if they impinged on an intact social system.

III

We are now in a position to form an idea about the various possibilities concerning the capitalist order's survival in the postwar world. It is first necessary to visualize the economic and political situation that will confront the dominant political groups at the end of the war. In what follows we shall confine ourselves mainly to the United States and consider no other case but that of complete victory.

Everybody is afraid of a postwar slump, threatening from a drastic reduction of military expenditure financed by inflationary methods as well as from mere reorientation of production. The all but general opinion seems to be that capitalist methods will be unequal to the task of reconstruction. This opinion in itself will be a political factor of first-rate importance. All the more essential is it to understand its rationale.

Viewed as a purely economic problem, that task might well turn out to be much easier than most people believe. It may happen that peace will be preceded by a period of decreasing war expenditure and of gradually increasing production for civilian consumption and also that the former will continue, though at a reduced rate, on a level much beyond that of prewar times. Either of these possibilities would greatly facilitate transition. But in any case, the wants of impoverished households will be so urgent and so calculable that any postwar slump that may be unavoidable would speedily give way to a reconstruction boom. Capitalist methods have proved equal to much more difficult tasks.

Nevertheless the opinion that the capitalist solution of the

problem will prove unworkable or, at all events, unsatisfactory, may well be true. For, like any other system, capitalism cannot be expected to function efficiently except on its own terms, that is to say, in a social atmosphere that accepts its responsibilities and incentives and allows it sufficient freedom of action. As we have seen, however, such an atmosphere and the corresponding attitude of public authority have not existed for some time, do not exist now and are obviously unlikely to exist in future. Capitalist management would hence have to solve the problems of reconstruction at home and abroad in the face of public antagonism, under burdens which eliminate capitalist motivation and make it impossible to accumulate venture capital, with risks of borrowing greatly increased,* without authority in the plant, and under the close control of a hostile bureaucracy. Deadlock so complete as to practically impose socialism as the only alternative is not inconceivable, but even conditions far removed from deadlock may preclude performance comparable to that of the past.

To be sure, a temporary revulsion of public sentiment in favor of laissez faire is not unthinkable. I need hardly stay however in order to show how very improbable it is. The public mind has renounced allegiance to the capitalist scheme of values. Private wealth is under a moral ban. All those bars to the effective functioning of capitalism embody what to most of us are cherished achievements. In particular,

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* High or progressively high taxation of profits increases the risks of borrowing for purposes of long-run investment, because it absorbs profits the accumulation of which might be counted on to take care of subsequent losses.

reduction of the fiscal burdens imposed upon the high income brackets and upon large-scale business and the removal of administrative fetters would be highly unpopular and could hardly be carried to the requisite extent in a situation in which high rates of taxes on all incomes will continue to be necessary. Intellectuals and organized labor will emerge from the war in a radical frame of mind. Nobody will dare and, what is more, nobody will care to advocate what would have to be a return not only to prewar conditions but - substantially - to the conditions of 1929.

Nor will there be a motive for any of the political groups of significant importance to influence the public mind in a pro-capitalist direction. Any regime that may be established will have to court the farm group and to present attractive schemes of agricultural planning. Farmers therefore might not be actively hostile to partial reversal of anti-capitalist policies - especially if their views about railroads are taken account of - but they will see little reason why they should go out of their way for the sake of it. Organized labor will find it impossible to abandon any of the positions it has conquered even if some labor leaders should entertain some doubts as to their economic value. The stratum of small and medium-sized business still constitutes a significant factor which no regime can afford to neglect. But they can be satisfied without making any concessions to big business which embodies the achievements and the vital energies of the American economy.

Thus there is a reasonable chance that after the war the bureaucratic apparatus of the federal administration will hold its own. At the end of the war it will first of all be in possession. It will have out-

grown initial difficulties and be in something like working order. It will have consolidated its position and have acquired enormous power. It will be a factor in its own right and stand ready to deal with the postwar emergency as it dealt with the war emergency. Political forces strong enough to liquidate the organs of the war economy as they were in 1919 are not in sight. There seems to be no reason why these organs should not succeed in establishing themselves as permanent institutions especially as they will be in a position to serve the immediate interests of agriculture and of labor and hence derive support from these quarters. In this case a sort of classe dirigente may develop.

The nature, structure, and ideology of this managing class is not determined as yet. Many mutually exclusive possibilities exist both as to what it will eventually turn out to be and as to what it will eventually do. Disregarding all other aspects and placing ourselves on a purely economic standpoint, we may however, out of a mash in full process of fermentation, select a few typical ones each of which corresponds to the views and interests of some existing sub-group.

1. The most obvious possibility is that the economic principles of the period immediately preceding the war will be applied to postwar problems - being consolidated and developed, revised and extended, according to circumstances. In this case the policy of income-generating public expenditure would be continued, first in order to prevent or mitigate the postwar slump and after that as a permanent device for regulating the pulse of the nation's economic life. As the reader knows, this policy commands wide-spread support. The fear of the postwar slump may well

silence such opposition as may be said to exist. And groups with completely different ultimate aims may agree on it because it is the easiest way toward all of them and carries the further advantage that none of them need be mentioned in advocating it.

Theorists are in the habit of dealing with this policy in the abstract. But its nature and consequences depend upon the complementary policies with which it is linked. In the case under discussion, these are taxation high enough and progressive enough to prevent private accumulation and in consequence the possiblity that large-scale business should ever again, financially speaking, stand on its own feet and become independent of government; labor legislation that shifts questions of wages, hours, and factory discipline definitely to the political sphere; and strict regulation, enforced by the threat of prompt prosecution, of the behavior of big business in every respect. Under these conditions, public income generation will automatically become permanent, quite irrespective of the factors stressed by the theories framed to prove its necessity from causes inherent in the saving-investment process of capitalist society.

Such a system will no doubt still be called capitalism. But it is capitalism in the oxygen tent - kept alive by artificial devices and paralyzed in all those functions that produced the successes of the past. The question why it should be kept alive at all is therefore bound to be put before long. Such concessions about relief from war rates of taxation and so on as are within practical politics may temporarily change details of the picture and postpone the putting of that question, but cannot be expected to change essentials.

2. It will therefore be perfectly natural - in fact it may be a practical necessity - to take further steps toward state management.

To begin with, it is difficult to see what role will be left for non-public banking and finance in an economic world thoroughly dependent on government financing that is itself entirely independent of private voluntary saving. Government to be sure still goes through the motions of "borrowing" and "lending," pays and receives interest and so on. But the life has gone out of these forms and an administrative rationalization of what is actually being done could easily eliminate them. If we assume that capitalist methods will disappear gradually there will be a narrowing sphere of activity for banks as we know them also in the future. They may continue to keep accounts and to fill administrative functions for an indefinite time. But though this may facilitate transitions it does not alter the fact that, if we must stick to old words, government will develop into the sole banker.

Again, government spending as a permanent policy can hardly fail to develop in governmental planning of investment. In fact, its failure to do so would be quite uneconomical. If government expenditure is to be the point of the economic process it stands to reason that the productive effects propelled by that expenditure will in the end have to be directed by public authority. The government will from time to time have to proclaim a national goal which its expenditure is to serve - such as housing for the masses, completion of the electrification of the household, reorganization of the transport system and of urban life to make them fit the conditions created by the airplane and to define the ways in which and the extent to which each particular goal is to be appreached.

Finally there is also another reason for this. Whatever the outcome of the war, the postwar world will hardly be a place for privately controlled trade and industrial venture. As to the first, it is difficult to see how private enterprise could cope with the conditions created by the immense differences as between countries in monetary and real cost of production that have developed of late. From a purely commercial standpoint, and taking account of all the "rigidities" that will prevent adaptation, the United States might well be unable to export at all.* Quite apart from the political considerations that are bound to complicate the problem still further, international trade in commodities and services will have to be cut off from its old background of commercial calculation and be managed by political treaties, bilateral and multilateral. But this implies domestic state management as domestic management implies the public management of international economic relations.

As to the second, international industrial venture involving long-term investment, the need for government leadership, perhaps on lend-lease lines, in what will inevitably carry imperialist futures, is still more obvious. The spacious possibilities that open up under these heads should be noted not less than the sources such a system harbors of waste surpassing anything ever charged to the account of capitalism. It should also be noted that such a system leaves the managing bureaucracy

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* The roots of this difficulty are in the prewar situation. One of the most curious contradictions in New Deal policy was its attempt to "liberalize" foreign trade while erecting a rigid economic structure at home.

free to allocate to private business as much or as little room as may be desired. Just as the TVA, a national venture, let contracts to private firms, so a similar national venture on the Yangtse, though initiated by government and controlled by it, may parcel out individual jobs to capitalist firms. Therefore, on the understanding that the essence of the bourgeois economy will be absent from the picture, we may call this system Guided Capitalism.

3. Some measures of nationalization will almost inevitably suggest themselves in a system of the type just discussed. Moreover, other measures - perhaps the nationalization or municipalization of utilities, of insurance, of mines - will be rendered easy by public support. It is difficult to foretell how far this tendency will go. The term "nationalization" does not sound well to every ear and it may be that other means of establishing no less complete public control, even if less rational and fraught with more friction, might be preferred by the political groups that will be in power. But if the federal government should follow this line to a significant extent, and if it should try to run the nationalized industries according to the principles of business rationality, Guided Capitalism would shade off into State Capitalism, a system that may be characterized by the following features: government ownership and management of selected industrial positions; complete control of government in the labor and capital market; government initiative in domestic and foreign enterprise.

4. It will always be a matter of taste whether a given way of running the economic engine be called socialist or not. On the one

hand, disgruntled bourgeois spoke of socialism when the first municipal gas works and the first progressive income taxes put in appearance; on the other hand, socialist groups that are not "in on it" will never admit that anything not sanctified by Marxian Doctrine can possibly be genuine socialism. Moreover, people care so much more for words than they do for things, that acceptance or avoidance of the term socialism may be dictated by tactical considerations. In this country, these considerations seem to tell against rather than for it so long as no violent break is on the cards.

If, however, we agree that advance on any of the lines we have briefly surveyed comes within the definition of gradual socialization, the problem narrows down considerably. Any approach to socialism other than by continued extension of government control and expropriation of the upper strata by taxation would no doubt meet resistance from the farm interest and from small and medium-sized business. Neither would put up a life-and-death fight in order to prevent the nationalization of big business - say, the corporations owning assets amounting to 50 million dollars or more. But they presumably would fight against anything much more radical than this, particularly against anything which they recognized as a "revolution." Barring such a revolution which, while never impossible, cannot be expected to be successful, an amphibial state for the calculable future is certainly the most probable one. From a purely economic standpoint this may be regrettable. Such a state will suffer from a lot of friction and inefficiencies that a return to the capitalist alternative or a resolute adoption of the socialist one would save, and it will not command the full motive power of either. On the other hand, amphibial states conserve many human values that would perish in others. Thus there may be as little reason for the fears of some as there is for the hopes of others.

Preface to the Hebrew Edition

It is with great pleasure that I welcome the Hebrew edition of this book. I have not made any changes in the text. Whether I ought to have done so is for my readers to judge. My own views have not been altered by the events of the last three years and I do not wish to retract anything of what I wrote in 1942. It occurs to me, however, that my readers might be interested to know what I think of those plans that have been recently framed in "capitalist" countries in order to stabilize the working of the economic engine and in particular to guarantee "full employment." Since the invitation to write a preface for this edition affords me the opportunity, I shall try to show, as briefly as possible, how those plans fit into my picture of the social processes of our time.

It is both necessary and sufficient to confine ourselves to one example: the bill that has been introduced in the Senate of the United States, by Senators Murray, Wagner, Thomas, and O'Mahoney on January 22, 1945, usually referred to as the Murray bill, or Full-Employment bill.* At the time of

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* Senate 380, 79th Congress, 1st session. For the Statement presented by Senator Murray and for his speech, see Congressional Record of that date.

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writing (May 1945) it is impossible to say whether the bill will pass and, if so, what its definitive content will be. We take it up for discussion simply because it embodies, in a typical form, one of the most characteristic tendencies of our time. The essential point is this. The administration is to make periodic estimates of the available supply of labor and of the aggregate public and private expenditure (a) that is actually in prospect and (b) that would be necessary in order to provide, at the expected price level, employment sufficient to absorb that supply of labor. If the sum

(a) is smaller than the sum (b), then the administration is to work out a program of measures that will increase non-Federal expenditure and, if necessary, Federal expenditure by the amount of the difference; if the sum (a) is greater than the sum (b), the administration is to work out a program of measures that will prevent "inflationary dislocation." The resulting recommendations are to go to a special joint committee of both Houses which will report on them with a view to securing such legislation as may be required.

In order to appreciate this plan and to approve it -- as I personally do -- it is not necessary to accept the economic theory behind it. The sponsors of the bill and their advisers seem to me to place an undue amount of confidence into the mere mechanics of expenditures and in particular in the efficacy of governmental deficit expenditure. ~~All~~ But all that really matters is that the bill, if passed, would create machinery for coordinating and rationalizing the unwieldy mass of private and public ~~divisions~~ decisions that produce subsequent business situations, and for prompt preventive and remedial action.

Our purpose does not call for appraisal of the chances that this administrative and legislative apparatus will work successfully. Doubts on this score furnish, of course, the bulk of the objections to the plan, but we shall simply assume that it will work with ideal efficiency. Provided readers grant this assumption -- at least for the sake of argument -- we can turn to the only question that is relevant to the analysis of this book: which kind of economy will emerge if the Murray plan becomes law and is then acted upon consistently?

I have said that the framers of the bill place an amount of confidence in the powers of "expenditure" that seems to me unduly great. Nevertheless -- and this is entirely to their credit -- they are aware of deeper implications. Among the recommendations which they direct the

Preface to the Hebrew Edition

administration to make in the event that sum (a) is smaller than sum (b), they list "Federal policies and activities with reference to banking and currency, monopoly and competition, wages and working conditions, foreign trade and investment, agriculture, taxation, social security, the development of national resources . . . ." (Sec. 3, c) and "the distribution of national income" (Sec. 3, f). They are right. Expenditures by private and public agencies are but the results and symptoms of the operation of all these and many other factors which must be watched and managed if the economic doctor's treatment is to be more than mere dermatology. In particular, the labor and capital markets must be fully controled. For in the face of discrepant interests, the State will have to decide and to enforce its decision if deadlock is to be avoided. Nor is this all: avoidance of depressive situations attended by unemployment will in many cases inevitably imply that government give a lead to private business which in practice will be difficult to distinguish from giving directions and taking the responsibility for expansion in some and contraction in other lines. Workmen, too, will have to be directed into the desired occupations and locations. No doubt this may be done in a very gentle way and in a spirit of cooperation rather than of dictatorship. I do not mean for a moment to suggest that the sponsors of the bill were insincere in holding out an olive branch to private business -- which they did in the bill's prefatory Declaration of Policy -- but I do mean to suggest that behind the cooperation stands compulsion, at least as a last resort, and that the logic of things will see to it that all the major decisions about what to produce, how to provide, at what prices, wages, and profits to produce will tend to pass from the private to the public sphere.

In the economy of the United States, capitalist interests and the capitalist scheme of economic and cultural values are not yet atrophic. The Murray bill is neither intended to change this economy into a socialistic one,

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nor could it do so if it were. But -- remember: we are not only assuming, for the sake of argument, that the bill passes but also that the machinery which it would create in this case uses to the full all the possibilities enshrined in it which is, perhaps, a most unrealistic assumption -- it will crystallize a transitional stage -- the stage I call Guided Capitalism -- which is no nearer to intact capitalism than it is to straight socialism. It is typically a midway house -- a midway house with a capitalist façade and a socialist basement. Of late, the plans of many such midway houses have been designed. Whether we like them or despise them, they may prove inhabitable for longer or shorter periods, according to circumstances. More significant than anything else about them is the very fact that they are being designed in quantity. I will make bold to say that this fact seems to me to verify the diagnosis of our time which the reader will find in this book.

Joseph A. Schumpeter

Cambridge, Mass., May 1945

Preface to the Hebrew edition, handwritten, typewritten

Hamburn Memoir on John M. Keynes

7/11

Dear Mrs Hope,

Here, at long last, is the Ms of my Memoir on Keynes. Please type it at your earliest convenience (1 carbon) and send me the ~~original~~ First copy and the carbon, keeping the Ms itself with you as a last resort in case of loss.

I certainly do not object to the 10 percent increase in your hourly rate.

The bill for $160 I have signed and sent off.

Before long I hope to send the ms. of the new Preface and the new chapter of my Capitalism etc.

I am working like a nigger and this glorious June is wasted so far as I am concerned.

Poor Elizabeth has the devil of a cold. I try to assert my authority – shaking in my shoes with fright – to keep her in bed but no such luck!

With kind regards

Yours ever

J A Schumpeter

John Maynard Keynes.
1883 - 1946.

by

Joseph A. Schumpeter

I

In his sparkling essay on the Great Villiers Connection

the essay (a review of W. F. J. Jun, Studies in Hereditary Ability) was published in The Nation and Athenaeum, March 27, 1926, and reprinted in the volume Essays in Biography, 1933. This volume gives more ~~[illegible]~~ ~~[illegible]~~ than does any other publication of his. ~~and~~ I shall accordingly refer to it more than once. Keynes the man and Keynes the scholar

Keynes showed a sense of the importance of hereditary ability — of the great truth, to use Karl Pearson's phrase, that ability runs in stocks — that fits but ill into the picture many people seem to harbor of his intellectual world. This obvious inference about his sociology is strengthened by the fact that in his biographical sketches he was apt to stress ancestral backgrounds with an unusual care. He would therefore understand my regret at my inability, owing to lack of time, to probe into the past of the Keynes connection. Let us hope that someone else will do this, and meanwhile content ourselves with an admiring glance at the ~~[illegible]~~ parents. He was born on the 5th of June 1883, the eldest son of Florence Ada Keynes, daughter of the Rev. John Brown D.D., and of John Neville Keynes, Registrar of the University of Cambridge — a mother of quite exceptional ability and charm, ~~a [illegible]~~ one time mayor of Cambridge, and a father who ~~[illegible]~~ is known to all as an eminent logician and author, among other things of one of the best methodologies of economics ever written.

+) Footnote next page

~~[illegible]~~

~~[illegible]~~

~~[illegible]~~

→

And let us note the ~~implications of the~~ academico-clerical background of the subject of this Memoir.

The implications of this background — both the eminently English quality of it and the century element in it — become still ~~by emphasis~~ clearer when we add two names: Eton and King's College, Cambridge. No new line!

→ Lord Keynes displayed his sense of the importance of hereditary quality by preserving in some case the main facts about his heroes' lineage and the implications of this habit (or what may be called his sociology) are fully brought out in his essay on the Great Villiers Connection. +)

+) See Essays in Biography, 1933.

would therefore indeed not approve any wish that someone should do this for him and that in particular some friend of his family should give us a picture of those excellent parents and their ancestral environment which is so representative of what had made for Eyland's greatness. At the moment, I cannot do more than invite the reader's attention to the academico-clerical background of the subject of this memoir.

~~This background – but the emotionally English quality of it at the gentry element in it – may be further emphasized by two names: Eton and King's College, Cambridge.~~

No new paragraph

Most of us are teachers and teachers are ~~prone~~ apt to exaggerate the formative influence of "education". But nobody will equate Eton tolerance. Moreover there is nothing to show that John Maynard's reaction to either place was anything but positive. He seems to have enjoyed a thoroughly successful scholastic career. In 1905 he was elected President of the Cambridge Union. In the same year he emerged as twelfth Wrangler. [Mathematicians will notice the latter distinction which cannot be attained without ~~[illegible]~~ some aptitude for mathematics plus ~~a~~ hard work – work hard enough to make it easy for a man who has gone through that discipline to acquire any more advanced techniques he may wish to master. They will recognize the →

→ mathematical quality of mind that underlies the purely scientific part of Keynes's work, perhaps also the traces of self-forgotten training. But some of them may under why be kept aloof from the current of mathematical economics which ~~[illegible]~~ ~~momentum~~ ~~[illegible]~~ at first about ~~for~~ the time when he first entered the ~~[illegible]~~ field. Nor is this all. ~~That he~~ Though never definitely hostile to mathematical economics – he even accepted the Presidency of the Econometric Society – ~~[illegible]~~ ~~[illegible]~~ never threw the weight of his authority ~~[illegible]~~ into its scale. The advice that emanated from him was almost invariably negative. Occasionally his conversation revealed something akin to doubt. But the explanation is not far to seek. The higher ranges of mathematical economics are in the nature of what is ~~[illegible]~~ in all fields referred to as "pure science". Results ~~[illegible]~~ have little bearing – not as yet, in any case – upon practical questions. But from the first to the last, it was political questions, ~~of practical~~ questions of policy, that all but monopolized Keynes's brilliant abilities. He was much too cultivated and much too intelligent ~~[illegible]~~ to despise logical niceties. To some extent he enjoyed them; to a still greater extent he bore with them, ~~impatience~~; but beyond ~~this~~ a boundary which it took him not long to reach, he lost patience with them. L'art pour l'art has no part of his ~~[illegible]~~ scientific creed. Wherever else he may have been progressive, he was not a progressive in analytic method. ~~The~~ The same holds in other respects that are unconnected with the use of higher mathematics. If the purpose seemed to justify it he had no objection to using ~~an~~ arguments →

Not were so candle as those of Sir Thomas More.

II

An Englishman, the adult son of a family from Eton and Cambridge, ~~the~~ passionately interested in the policy of his nation, who had conquered the presidential chair of the Cambridge union in the symbolic year 1905 ~~that~~ ~~the spectacular victory of Campbell-Bannerman's~~ marked the passing of an epoch and the dawn of another ~~and youthful mind~~ [1]. Why did such an Englishman and embark upon a political career, why did he go to the India Office instead? Many pro's and con's ~~and also many random factors of chance~~ enter into a decision of this kind, but there is one point about it which it is essential to grasp. Nobody could ever have talked to Keynes for an hour or ~~that~~ discovering that he was the most unpolitical of men. The political game as a game interested him no more than did racing-or, for that matter, pure theory per se. With great musical gifts for debate and ~~for~~ with a keen perception of tactical values, he yet seems to have been ~~quite~~ impervious to the lure - or the anything like as strong as it is in England - of the charmed circle of political office. Party meant little or nothing to him. He was ready to cooperate with anyone who offered support for a reconsideration of his (and to forget, at a moment's notice, any past passages of arms). But he was not ready to cooperate with anyone on any other terms, let alone ~~or in part~~ alone to accept anyone's leadership. His loyalties were loyalties to measures, not loyalties to individuals or groups. But still less than a respecter of persons was he a respecter of creeds or ideologies or flags.

[1] The Campbell-Bannerman era too, and a parliamentary Labour Party emerged in January 1906.

Was he not therefore cut out for the role of an ~~great~~ ideal civil servant, by nature made to become one of those great ~~Cyphers~~ ~~underlings~~ permanent undersecretaries of state whose discreet influence counts for so much in the shaping of England's recent history? Anything but that. He had no taste for politics, but he had less than no taste for patient routine work and for breaking in, by gentle arts that refractory wild beast, the politician. Under these two negative propensities, the aversion to the ~~storm of the~~ political arena and the aversion to ~~the dust of offi~~ red tape, propelled him toward the role for which he was indeed by nature made, ~~and~~ for which he quickly formed the form that suited him to perfection, and from which he never departed throughout his life. Whatever we may think of the ~~term~~ Psychological Laws ~~which~~ which he was to formulate ~~were perhaps unduly fixed~~, we cannot but feel that from an early age he thoroughly understood his own. ~~the psychological law of his own career~~ This is in fact one of the major keys to the secret of his success ~~of all~~ ~~Tell us any questions?~~ ~~To his success or greatness~~ ~~the secret~~ ~~of his happiness~~ ~~and~~ also to the secret of his happiness: For unless I am much mistaken his life was an eminently happy one. ~~happi~~

~~In a sense therefore he was eminently qualified to make an ideal civil servant, to become a permanent undersecretary of state. He might have been a useful to a political minister's prayer. But not only was he too independent for that – of this he gave proofs before long – he also had no taste for the current tasks of administration.~~

After two years at the India Office (1906–8) he went back to his University, accepting a fellowship at King's (1909), and quickly established himself in the circle of this Cambridge fellow economists. He taught straight Marshallian doctrine with the 5th book of the Principles as the center, the doctrine that he mastered as few people did and with which he remained identified for nearly years to come. ~~His teaching (after~~ ~~Pigou~~ A picture survives in my memory of how he then looked to a casual visitor to Cambridge – the picture of the young teacher of spare frame, ascetic countenance, flashing eyes, intent and tremendously serious, vibrating with what seemed to that visitor suppressed impatience, a formidable controversialist whom nobody could overlook, everybody respected, and some liked.+) His rising reputation is attested by the fact that as early as 1911 he was appointed editor of the Economic Journal in succession to its first editor, Edgeworth. This key position in the world of economists he filled for 27 years until spring 1945 +) – considering the length of his tenure of the office – with unflagging zeal. Edgeworth served once more, as joint editor, 1918–1925. He was succeeded by D. H. Macgregor who served 1925–1934 (at first as assistant, then as joint editor) to be in turn succeeded by Mr E.A.G. Robinson (who has been appointed assistant editor in 1937)

+) My own acquaintance with Keynes, productive of a totally different impression, dates only from 1927.

footnote to not previous page

+) Once he patiently explained to a foreign contributor that while it is permissible to abbreviate exempli gratia into e.g., it is not permissible to abbreviate for instance into f.i. – and would the author sometimes the alteration?

But all the other interests and avocations in the midst of which he filled it, his editorial performance is truly remarkable, in fact almost unbelievable. It was not only that he shaped the general policy of the Journal (and of the R. Economic Society of which he was secretary.) He did much more than this. Many articles grew out of his suggestions, all of them received, from the ideas and facts presented down to punctuation, the most minute critical attention.+) +) But, in some cases, the finished product was as much his as the author's. (We all know the results and everyone of us has no doubt his own opinion about them. But I feel confident of speaking for all us when I say that, taken as a whole, Keynes the editor has had no equal ever since Dupont de Nemours managed the Éphémérides.

The work at the India Office was not more than an apprenticeship that would have left for traces in a less fertile mind. It is highly revelatory not only of the vigor but also of the type of Keynes's talent. Yet it bore fruit in his case: his first book – and first success – was on Indian Currency and Finance.*) It appeared in 1913 when he also appointed member of the R. Commission on Indian Currency and Finance (1913–9). It is fair, I think, to call this book the best English work on the gold-exchange standard, in spite of its particularity. However, it will prove interesting to attend to another question that is but distantly related to the merits of this performance taken by itself: can we discern in it anything that points toward the General Theory? In the preface to the latter Keynes himself claimed not more than that his teaching of 1936 seemed to him "a natural evolution of a line of thought which he had been pursuing "for several years". On this I shall offer some comments later on. But now I will make bold to assert that, though the book of 1913 contains none of those characteristic propositions of the book of 1936 that have been felt to be "revolutionary", the general attitude taken towards monetary phenomena and monetary policy by the Keynes of 1913 differs clearly from that of the Keynes of the Treatise (1930). Monetary management was then no novelty of course – which is just the point at issue.

*) In 1910–11 he gave lectures on Indian Finance at the London School of Economics, see Hayek, The London School of Economics 1895–1945, Economica, February 1946, p. 17.

From an unpublished Memoir on John M. Keynes

precisely why it should not have been heralded as a novelty in the 20s and 30s — and preoccupation with ~~equilibrium~~ Indian problems + so particularly likely to induce awareness of its nature, necessity and possibilities. But Keynes's vivid appreciation of its bearing upon prices, exports and imports, ~~production~~ and employment was ~~yet~~ nevertheless something new, something that, if it did not uniquely determine, yet conditioned his own ~~advance~~ line of advance. ~~He must~~ Moreover we must remember how ~~closely~~ his theoretical development in posterior times was related to the particular situations in which he offered practical advice and which neither he nor anyone else foresaw in 1913: add theoretical ~~of the events in the 20s~~ of the English experience in the 20s to the theory of Indian Currency of Finance and you will get ~~substantially~~ the substance of the Keynesian ideas of 1930. This statement is conservative. I could go further — a little — were I not afraid of falling into an exercise ~~that is very common among~~ biographers.

that is very common among

III

In 1915, the potential public servant in the academic form turned into an actual one: he entered the Treasury. English finance during the first world war was eminently "sound" and spelled a moral performance of the first order. But it was not conspicuous for originality, and it is possible that the brilliant young official then acquired his dislike of the Treasury Mind and the Treasury View that became so marked later on. His services were however appreciated for he was chosen to serve as Principal Representative of the Treasury at the Peace Conference which might have been a key position if such a thing could have existed within the orbit of Lloyd George — and also as Deputy for the Chancellor of the Exchequer on the Supreme Economic Council. More important than this, speaking from the biographer's standpoint, is his abrupt resignation in June 1919 which was so characteristic of the man and of the kind of public servant he was. Other men in the English and American staffs had much the same misgivings about the peace. But of course they could not possibly speak out: there was such a thing as etiquette and another thing they lived to call duty; there were those small loyalties in the service of men's souls from being saved; there was the lust of all the other motivating considerations, human and all-too-human, however all of them, that keeps leads from being done. But Keynes was made of different stuff. He went and told the world why. He went and leapt into international fame.

7

The Economic Consequences of the Peace (1919) met with a reception that makes the word Success sound commonplace and insipid. Those who cannot understand how luck and merit intertwine will no doubt say that Keynes simply wrote what was on every sensible man's lips; that he was very favorably placed for making his protest resound all over the world; that it was this protest as such and not his particular arguments that won him every ear, and that at the moment the book appeared the tide was already running on which it was to ride. There is truth in all this. Of course, there was an unique opportunity. But if he chose, on the strength of this, to deny the greatness of this feat he had better delete this phrase altogether from the pages of history. For there are no great feats without preexisting great opportunities. ~~And [illegible] a great opportunity [illegible]~~

Simply the feat was one of moral courage. The details of the book's performance, displayed and analyzed in A Revision of the Treaty (1922), do not call for notice here. But there are some points about it that do. First, we get an additional glimpse of Keynes the public servant, namely, of his attitude to ~~official~~ political chieftains+). He rightly sensed

+) The relevant passages, masterpieces of artistic economy, are republished in Biographical Essays.

Primarily the feat was one of moral courage. But the book is a masterpiece — packed with practical wisdom that never lacks depth; ~~positively~~ logical yet never cold; genuinely humane but nowhere sentimental; meeting all facts without vain regrets but also without hopelessness; sound advice ~~analysis~~ addressed to sound analysis advice ~~[illegible]~~ ~~and matter fitting each other to perfection~~ that it is a work of art. Form and matter fit each other to perfection. Everything is to the point and there is nothing in it ~~redundant~~ that is not to the point*. ~~The very brilliance of the exposition [illegible]~~ No idle* adornment disfigures its wise economy of means. The very polish of the exposition — never again to be quite so well-brings out its complexity. ~~[illegible]~~ ~~to [illegible] again [illegible] it [illegible]~~ The passages in which Keynes tries to explain, in terms of the dramatis personae, the tragic failure of that pivotal conference, he rises to heights that have been touched by few.

*) See pp 26-50, on the Council of Four, republished, with an important addendum, the Fragment on Lloyd George, in the Essays in Biography. It is painful to report that, at the time, some opponents of Keynes's views, in full retreat before his victorious logic, seem to have resorted ~~[illegible]~~ to sneers about ~~Keynes's~~ his presentation of certain facts and interpretation of motives neither of which, so they averred, he was in a position ~~[illegible]~~ to judge. Since this indictment of Keynes's veracity has

→ been recently reprinted in a concise pamphlet in an American magazine, it is first of all necessary to ask the reader to satisfy himself that not a single result of Keynes's analysis and not a single ~~of his~~ recommendation of his depends on the correctness or incorrectness of the picture he drew of the moves and attitudes of Clemenceau, Wilson and Lloyd George. But seeing, since it is part of the purpose of this Memoir to delineate ~~it~~ a character, it is further necessary to prove that there is absolutely no foundation for the supposition that Keynes indulged in a flight of "poetic fantasy" and that he pretended to ~~have~~ an intimate knowledge of "arcana" that cannot have been known to him — which, at ~~the~~ best, would convict him of pettiest vanity and, at worst, of more than that. But the proof in question is not difficult to supply. If the reader ~~will~~ will refer to that masterly sketch, as I hope he will, he ~~will~~ is bound to find that Keynes ~~didn't~~ claimed no personal intimacy ~~with~~ or, ~~with the exception of Lloyd George, any personal acquaintance~~ with those three men and personal acquaintance only with Lloyd George. He said nothing about the private meetings of the four (the fourth was Orlando) but merely described scenes at the regular meetings of the Council of Four* which, along with all other leading experts, he must have normally attended in his official capacity. Moreover, his presentation of the personal aspects of the steps that led to the disastrous result is amply supported by independent evidence: this brilliant story is nothing but a reasonable interpretation of a cause of events that is common knowledge. Finally, critics had better bear in mind that this interpretation is distinctly generous and perfectly free from traces of any resentment, however justifiable, that Keynes may have felt.

The economics of the book as well as of *A Revision of the Treaty* (1922) that complements and in some respects amends its argument, are of the simplest and did not call for any special technique. ~~The model of the old up marketing free and of progressive reason.~~ Nevertheless there is something about it that calls for our attention. ~~because it illustrates the continuity of its author's thought.~~ Before embarking on his great venture in persuasion, Keynes ~~[illegible]~~ drew a sketch of the economic and ~~[illegible]~~ social background of the political events he was about to survey. With but slight alterations of phrasing this sketch may be summed up like this. Laissez-faire capitalism, that "extraordinary episode" had come to an end in August 1914. The conditions were rapidly passing in which entrepreneurial leadership was able to secure success after success, propelled as it had been by rapid growth of populations and by abundant opportunities to invest that were incessantly recreated by technological improvements and by ~~[illegible]~~ a series of conquests of new sources of food and raw materials. Under these conditions there had been no difficulty about absorbing the savings of a bourgeoisie that kept on baking cakes "in order not to eat them". But now (1920) these impulses were giving out, the spirit of private enterprise was flagging, investment opportunities were vanishing, and ~~[illegible]~~ →

longer saving habits of thrifty people ~~lead to this social formation~~; ~~their~~ persistence actually made things worse than they need be. Here then we have the origin of the modern stagnation thesis – as distinguished from the one that we may, if we have done, find in Ricardo. And here we also have the embryo of the General Theory. Every comprehensive "theory" of an economic state of society consists of two complementary but essentially distinct elements. There is first the theorist's vision (or apparition) about the basic features of such a state, about what is and what is not important in order to understand its life at a given time – let us call this his Vision; and there is second the theorist's technique by which he conceptualizes his vision and which turns the latter into concrete propositions or theorems. In these pages of The Economic Consequences of the Peace we find nothing of the theoretical apparatus of the General Theory. But we find the shell of the vision of things social and economic of which that apparatus is the technical complement. The General Theory is nothing but the final result of a long struggle to make ~~these pages of [illegible]~~ that vision of our age analytically operative.

IV

~~For economists of the "scientific" type Keynes is of course the Keynes of the General Theory. In order to serve as much space as possible for the straight-line development of the "Tract" and by the "Treatise", I shall have to brush aside rattlingly many things that ought not to go unrecorded. Three foothills of his Consequences are however noticed in the note below +) and for facts must be sacrificed to =>~~

+) These are: his article on population and the ensuing controversy with Sir William Beveridge (Economic Journal 1923); his pamphlet, The End of Laissez-Faire, 1926; and his article on the German Transfer Problem in the Economic Journal, March 1929, with subsequent replies to the criticisms of Ohlin and Rueff. The first attempt to conjure Malthus's ghost – to defend (at the threshold of the period of unsalable masses of food and raw materials!) the thesis that since somewhere about 1906 nature had begun to response too generously to human effort and that overpopulation was the great problem, or one of the great problems of our time: perhaps the least felicitous of all his efforts and indicative of an element of recklessness in his makeup which those who loved him best cannot entirely deny. All that needs to be said about the End of Laissez-Faire is that we must not expect to find in this piece of work what the title suggests. It was not at all what the Webbs wrote in that book of theirs that

→

footnote goes on

invites comparison with Keynes's. The article on German reparations reveals another side of his character: it was evidently dictated by the most generous motives and by unerring political wisdom; but it not so easy to deal with that Ohlin and Ruff found it easy to deal. ~~It is difficult to understand how Keynes could have been blind to the weak spots in his argument.~~ But in the service of a cause he believed in he could sometimes, in noble haste, overlook defects in the narrow sense. — The volume entitled Essays in Persuasion, 1931, is perhaps the best method of studying the quality of his reasoning in the not-quite-professional part of his work.

Enemies and detractors neglecting the enthralling glamour of his personality, have naturally made the most of this element in his work. But all I can do, is to paraphrase with sorrow the difficulty of Goethe's: "Through the word I cannot share your warm feeling, I feel compelled call them lifeless."

→ A Treatise on Probability which (he published in 1921.)

There cannot be, I fear, much question about what Keynes means for the theory of probability; the question that is of interest to us is what the theory of probability meant for Keynes. Subjectively, it seems to have been an outlet for the energies of a mind that found not complete satisfaction in the problems of the field to which, as much from a sense of public duty as from taste, he devoted most of his time and strength. He entertained no very high opinion about the purely intellectual possibilities of economics. Whenever he wished to breathe the air of high altitudes he did not turn to our pure theory. He was something of a philosopher or epistemologist. He was interested in Wittgenstein. He was a great friend of that brilliant thinker who died in the prime of life — Frank Ramsey to whose memory he erected a charming monument in The New Statesman and Nation, October 3, 1931, republished in the Essays in Biography. To this essay, the most warm-hearted thing he ever wrote, is appended an anthology of gleanings from Ramsey's notes. These express Ramsey's views of course, and not Keynes's, but, for an occasion like this, nobody could choose passages that do not strike a sympathetic note. Thus, Ramsey's sayings become indicative of Keynes's philosophy.

→ But no merely receptive attitude ~~[illegible]~~ ~~productiveness~~ could have ~~satisfied~~ satisfied him. He had to have a flight of his own. It is highly revelatory of the texture of his mind that he chose probability for the purpose – a subject bristling with logical niceties yet not entirely without utilitarian connotation. His indomitable will produced what, ~~[illegible]~~ seen as I am trying to see it, was no doubt a brilliant performance where specialists, non-Cambridge specialists particularly might say. ~~And it is the best proof of his amazing gift for ability to detail [illegible] that today~~ [illegible] book.

We are drifting from the work to the man. Let us then use this opportunity for looking at him at little more closely. He had returned to King's ~~College~~ and to his previous pattern of life. But the pattern ~~though fundamentally it remained the same~~ was developed and enlarged. He continued to be an active teacher and research worker; he continued to edit the Journal; he continued to write the public cases his own. But though he strengthened his ~~[illegible]~~ ties with King's by accepting the all-important function of "Bursar", ~~a disinterested~~ the London home at 46, Gordon Square became second headquarters before long. He acquired an interest in and became Chairman of The Nation – which superseded the Speaker in 1921, absorbed the Athenaeum, and merged with The New Statesman (in 1931) – (The New Statesman and Nation) – to which he devoted the current stream of articles that would have been full-time work for some other man. Also, he became Chairman of the National Mutual Life Assurance Society to which he gave much time and skill, I believe though I am not sure, as his chief source of income ~~[illegible]~~ for some years. ~~He~~ →

No new paragraph!

There was no nonsense about him, in particular no nonsense about business ~~[illegible]~~ and money making; he frankly appreciated (in the 20s) the comfort of a proper establishment; and not less frankly he used to say that he would never ~~[illegible]~~ accept a professorial appointment because he could not afford to do so. ~~[illegible]~~ In addition to all this he served on the Economic Advisory Council and on the (Macmillan Committee) Committee on Finance and Industry. In 1925 he married Lydia Lopokova, a distinguished artist, who proved a ~~[illegible]~~ congenial companion and devoted helpmate to the end.

~~There is nothing unusual in~~ That combination of activities is not unusual. What make it unusual and indeed a marvel to behold is the fact that he put as much energy in each of them as if it had been his only one. His appetite and capacity for efficient work surpass belief, and ~~[illegible]~~ his power of concentration ~~[illegible]~~ on the piece of work in hand was ~~[illegible]~~ ~~It is [illegible] to mention it in addition to capacity for efficient work~~ truly Gladstonian: Whatever he did, he did with a mind freed from everything else. He knew what it is to be tired. But he hardly seems to have known dead hours of deadening ~~[illegible]~~ and faltering purpose. ~~[illegible]~~ ~~Even this fails to do justice to [illegible] organism. As a rule, there is [illegible] such [illegible] machines. They~~

Memoir on John M. Keynes

Insert paragraph:

~~On such subject~~

Nature is wont to impose two distinct penalties upon those who try to beat out their stock of energy to the thinnest leaf. One of these penalties Keynes undoubtedly paid. The quality of his work suffered from its quantity and not only as to form: most of his secondary work shows the traces of hurry, some of his most important work the traces of incessant interruptions that injured its growth. He fails to realize this – to realize that he has before himself work that has never been allowed to ripen, has never received the last finishing touch – will never do justice to his powers.+) But the other penalty was remitted to him.

+) The most obvious example for this is his most ambitious venture in research, the Treatise on Money which is a shell of several pieces of powerful but uninsisted work, very imperfectly put together. (see below, p. ...) But the instance that will convey my meaning best, is the biographical essay on Marshall (Economic Journal, September 1924). He evidently lavished love and care upon it. As a matter of fact, it is the most brilliant life ~~biography~~ of a man of science I have ever read. And yet the reader who turns to it will not only derive much pleasure and profit but also see what I mean. It starts beautifully, it ends beautifully, but in order to be perfect it would have needed another fortnight's full-time work.

In general, there is something inhuman about such machines that fully use every ounce of their fuel. Such men are mostly cold in their personal relations, inaccessible, preoccupied, a bore. Their work is their life, no other interests exist for them or only interests of the most superficial kind. But Rogers was the exact opposite of all this — the pleasantest fellow you can think of, pleasant, kind, and cheerful in the sense in which precisely those people are pleasant, kind, and cheerful who have nothing on their minds and whose one principle it is never to allow any pursuit of theirs to degenerate into work. He was affectionate. He was always ready to enter with friendly zest into the views, interests, and troubles of others. He was generous, and not only with money. He enjoyed conversation and shine in it. And, contrary to a widely spread opinion, he was polite, polite with an old-world punctilio that costs time. For instance he would refuse to sit down to his lunch, in spite of telegraphic and telephonic expostulations, until his guest, delayed by fog in the Channel, had put in appearance at 4 p.m. His "extracurricular" interests were many, and each of them he pursued with joyful alacrity. But this is not all of it. Once more, people are not uncommon who, in spite of absorbing avocations, enjoy some recreative activities in a passive way. The Rogersian Touch is that with him recreation was creative. For instance, he loved old books, niceties of bibliographic controversy, details of

Extract from Memoir on John M. Rogers

the characters, loves, and thoughts of men of the past. Marshall, perhaps the model of early p[illegible] for Tout, by the classical element of his education, still very apparent because he never parodied but still was a very important part of the formation of his mind [illegible] people who shared this taste which may have been fostered in him by the classical ingredient in his education. But whenever he developed it he took both like the workman he was and we owe to this hobby several not unimparted classifications and points of literary history.+) He also had a lover and up to a point a good judge of painting.

+) The literatures of philosophy and economics attracted him most. In this pursuit Professor Piero Sraffa became to him a much-appreciated ally. The best example I can offer of results is the edition of Hume's Abstract of his Treatise on Human Nature "reprinted with an Introduction by J. M. Keynes and P. Sraffa" 1938. The Introduction is a curious monument of philological ardor.

* to a modest extent also a collector of pictures. He thoroughly enjoyed a good play, and founded or helped to found the Cambridge theatre, apparently a creation out of nothing. Not anybody will forget who ever went to it. And, once upon a time, an acquaintance of his received the following note from him, evidently dashed off in high good humor: "Dear ..., if you want to know

that the moment exclusively occupies my Time, look at the enclosure." +) The enclosure consisted of a program or prospectus

+) The acquaintance, the most disorderly of humans, does not keep letters. The exact wording of Keynes's note can therefore not be verified. But I am positive that it contained a single brief sentence and that the import of this sentence was as stated. It must have been about ten or fifteen years ago.

(Perhaps more.)

of the "Camargo Ballet".

We are not yet ready to go on. Africa and the Good of Keynes's economics, ~~[illegible], though [illegible] there, at least in a general way, that [illegible] that he [illegible] pandering to the most stay for a [illegible] Because his [illegible] on all people took to [illegible] his [illegible] — [illegible] primarily responsible for his prominority [illegible] and his unpopularity with others. Still more because his technical economics is [illegible] understandable without it, we must [illegible] for [illegible] not indeed [illegible] to dispense it — for [illegible] sufficiently [illegible] there, at least in a general way —

~~[illegible] Keynes's [illegible] are [illegible] contradictory [illegible] But [illegible] not only the good [illegible] which he always looked but [illegible] also the starting point of his analytic work~~

V.

~~I propose to the straight-angle development of Keynes's economic thought that leads from the Consequences to the General Theory~~

I return to the highway. ~~I thought that leads straight from the Consequences to the General Theory.~~

As stated above, our first stop is at the Tract on Monetary Reform (1923). Since, with Keynes, Practical Advice was the goal and beacon light of analysis I will do what in the case of other economists I should consider an offence to do, viz., (initiate readers to) first look at what it was he advocated. It was, in substance, stabilization of the domestic price level for the purpose of stabilizing the domestic business situation, secondary attention being paid also to the means of mitigating short-run fluctuations of foreign exchange. In order to achieve this he recommended that the monetary system created by the necessities of warfare should be carried over into the peace economy, the keystone of the various suggestions offered being ~~the sepa~~ - with a trepidation quite unlike him - being the separation of the note issue from the gold reserve which he wished however to retain and of which he was anxious to emphasize the importance.

There are two things in this piece of advice that should be carefully noticed. First, its specifically English quality;

second, ex vision of England's short-run interests and of the kind of (English) man the adviser was, its price was dim and conservative.

It cannot be emphasized too strongly that Keynes's advice was in the first instance always English advice, born of English problems even when addressed to other nations. Barring some of his artistic tastes — Mlle. Camargo had not ~~of course~~ been an Englishwoman (of course) — he was surprisingly insular, even in philosophy, but insular so much as in economics. But, he was fervently patriotic — of a patriotism ~~that~~ which was indeed quite untinged by vulgarity but was so genuine as to be subconscious and therefore all the more powerful (to impart a bias to his thoughts and) to exclude full understanding of foreign (also American) viewpoints, ~~interests~~, conditions, interests, and especially needs. Like the old free-traders, he always ~~generally~~ (called) what was (at any moment) truth (and tried to impose) for England into truth and wisdom for all times and places. But this is not all of it. In order to locate the standpoint from which his advice was given it is further necessary to remember that he was of the high intelligentsia of England, unattached to class or party, a typical product of its tradition, the rightly claimed spiritual kinship with the Locke-Mill Connection.

What was it, then, that this patriotic English intellectual believed? The generalizations we have already noticed in the pages of the Consequences. But England's case was more specific than that. She had not emerged from the war as she had emerged from the war of the Napoleonic era. She had emerged impoverished.

he had lost many of his opportunities for ~~good~~ the moment and some of them for good. Not only this, but his social fabric had ~~[illegible]~~ been weakened and had become rigid. His taxes and rego-rates were incompatible with vigorous development, yet there was nothing that could be done about it. Keynes was not given to vain regrets. He was not in the habit to bemoan what could not be changed. Also he was not the sort of man who could bend his mind to the individual problems of coal, textiles, steel, shipbuilding (though he did offer some advice of this kind in his current articles). Least of all was he ~~[illegible]~~ the man to preach regenerative creeds. He was the English intellectual, belonging a most uncomfortable situation. He was clothed and his philosophy of life was essentially Victorian philosophy. So he turned resolutely to the only parameter of action that seemed left to him, both as an Englishman and as the kind of Englishman he was — monetary management. ~~[illegible]~~ ~~[illegible]~~ Perhaps he thought that it might heal. He knew for certain that it could soothe — and that satisfactory ~~[illegible]~~ to a gold system at never parity was more than his England could bear.

If only people could be made to understand this they might also understand that ~~[illegible]~~ practical Keynesianism is a seedling that cannot be transplanted into foreign soil; it dies there and becomes poisonous before it dies. ~~[illegible]~~ ~~[illegible]~~ ~~[illegible]~~

But in addition they could understand that, left in English soil, this seedling is a healthy thing and promises both fruit and shade. Let me say once and for all: all this applies to every bit of advice that Keynes ever offered. For ~~[illegible]~~ the rest, the monetary mechanism of the Tract was anything but revolutionary. ~~But~~ There was however a novel emphasis on it as a means of general economic therapeutics. ~~[illegible]~~ And concern with the saving-investment mechanism is indicated in the first lines of the preface and throughout the first chapter.+) Thus though the

+) See e.g. the highly characteristic passages on p. 10, and also the description of the "investment system" on p 8 which anticipates some of the very inadequacies of the analysis of the General Theory. Even then, and indeed from first to last, Keynes displayed a curious reluctance to recognize a very simply and obvious fact and to express it by the in less simple and obvious phrase, typically industry is financed by banks. immediate task before the author prevented him from going very far into these matters, the book does indicate further ~~up~~ advance towards the General theory.

Analytically, Keynes accepted the Quantity Theory which "is fundamental. Its correspondence with facts is not open to question" (p. 84) All the more important is it for us to realize

that this acceptance, resting as it does on the very common confusion between the quantity theory and the equation of exchange, meant much less than it seems to mean exactly as Keynes's later repudiation of the quantity theory means much less than it seems to mean. What he intended to accept was the equation of exchange — in its Cambridge form — which, whether defined as an identity or as an equilibrium condition does not imply any of the propositions characteristic of the quantity theory in the strict sense. Accordingly, he felt free to make velocity — or its equivalent in the Cambridge equation — a variable of the monetary problem, very properly giving Marshall for his "development of the traditional way of considering the matter" (p.86). This is the Liquidity Preference in embryonic form. Keynes overlooked that this theory can be traced back to Cantillon — at least — and that it had been developed, though sketchily, by Kemmerer,+)

+) E.W. Kemmerer, Money and Credit Instruments, 1907, p. 20. ≠ But on p. 193 of the Tract, Keynes commits himself to the untenable statement that "the national price level is mainly determined by the amount of credit created by the banks" and from this he never departed. To the end, M remained for him an independent variable, given to the economic process, though determined not by gold production as in the age of old but either by the banks or by the "monetary authority" (Central Bank or Government). This however — considering M as "given" — is one of the characteristic features of the quantity theory in the strict sense. Hence my statement in the text that he never abandoned the quantity theory as completely as he thought he did.

who said that "large sums of money are continually being hoarded" and that "the proportion of the circulating medium which is hoarded ... is not constant." We cannot go into the many excellent things in the Tract, e.g. the masterly sections* on The Forward Market in Exchanges (Chapter III, section IV) and on Great Britain (Chapter V, section I) which it is impossible to admire too highly. We must hurry on to our "second stop" on the road to the General Theory, the Treatise on Money (1930).

Apart from the exception of the Treatise on Probability, Keynes never wrote another work in which the hortatory purpose is less visible than it is in the Treatise on Money. It is there, all the same, and not confined to the last Book (VI) in which, among other things, we find all the essentials of Bretton Woods — that extraordinary achievement. Primarily however these two volumes are Mr Keynes's most ambitious piece of genuine research, of research so brilliant and yet so solid that it is a thousand pities that the harvest was garnered before it was ripe. (~~There is a passage in Keynes's Memoir of Marshall that he who runs to look below the surface will find petition (Essays, pp. 211-2~~) If only he had learned something from Marshall's craving for "improvable perfection" instead of lecturing him about it! (Essays in Biography, pp 211-2). Moreover, Professor Myrdal's gentle ~~sneer at it is both fair — or where is its equal? Professor Myrdal's gentle sneer~~

* A semi-apologetic passage in the Preface of the Treatise shows that he was not unaware of the fact that he was offering half-baked bread.

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v. note — II 209 ~~[illegible]~~ 1 [illegible]
II 209

That that "attractive Anglo-Saxon kind of unnecessary originality" is amply justified". Nevertheless, the book was

+) Gunnar Myrdal, Monetary Equilibrium (English translation, by Bryce and Stolper, 1939, of a German version of the Swedish original that appeared in the Ekonomisk Tidskrift in 1931) p. 8. Myrdal's protest was not, of course, made on his own behalf ~~[illegible]~~ but on behalf of ~~the~~ Wicksell and the Wicksellian group. But a similar protest would have been in order on behalf of Böhm-Bawerk and his followers, especially of Mises and Hayek, & the latter's Geldtheorie & und Konjunkturtheorie had, it is true, been published ~~appeared~~ only in 1929. But Böhm-Bawerk's work was available in English and ~~so [illegible] 1896~~ Taussig's Wages and Capital dates from 1896. Nevertheless ~~the~~ Keynes wrote the capital theory of Book VI exactly as if they had never lived. But there was no obligation in this. He simply did not know. Proof of his good faith is the ample credit he gave to all authors he did know, Pigou and Robertson among them. → the outstanding performance in this field and day. All I can do here is to collect the most important ~~points~~ signposts that point toward the General Theory. ++) →

++) This of course involves injustice to the book as a whole, and in particular to the first two books: the conventional but nonetheless brilliant ~~An~~ introduction (Nature of Money, book I) and the almost independent treatise on price levels (Value of Money, book II) which is full of suggestive ideas. It must be remembered — which is really the most ~~important~~ fundamental difference between the treatise and the General Theory — that the work (purposes to be ~~is particular~~) an analysis of the dynamics of price levels, "of the way in which the fluctuations of the price level actually came to pass" (Vol I p. 153), though (in reality it is much more than this.

There is, first, the conception that was to be fully developed in the General Theory, of the theory of money as the theory of the economic process as a whole. This conception is, second, embedded into the vision or diagnosis of the contemporaneous state of the economic process that never dawned from the consequences on Thrift, saving and investment decisions are resolutely separated quite as resolutely as in the General Theory, and the ~~[illegible]~~ minute thrift is well established in the role of villain of the piece. The recognition extended to the work of "Mr J. A. Hobson and others" (Vol I, p 179) is highly revelatory in this respect. And we learn that ~~*~~ a Thrift Campaign is not the way to bring down the rate of interest (~~*~~ e.g. Vol II, p 207). Differences ~~*~~ in conceptualization - sometimes only in terminology - obscure but to not diminish the fundamental identity of the ideas the author strives to ~~explain~~ convey. Thus, fourth, much of the argument runs in terms of the Wicksellian divergence between the ~~many~~ "natural" and the money rate of interest. To be sure, the latter is not yet the rate of interest, and neither the former nor ~~[illegible]~~ profits are "yet" turned into the "marginal efficiency of capital". But the argument clearly suggests both. Fifth, the emphasis upon expectations, upon the "bearishness" that is not yet Liquidity Preference from the the speculative motive, the theory that the fall in money wage rates ~~[illegible]~~ in depression ~~[illegible]~~ will (reduction in the rate of efficiency-earnings") will

Memoir on John M. Keynes

tend to reestablish equilibrium if and because it will act on interest (bankrate) by reducing the requirements of Industrial Circulation — all these and many other things read like imperfect and embarrassed ~~experiment of~~ (first) statement of General-Theory propositions — not to mention bananas, widow's cruse, Danaid's jars.

Transcription on John M. Keynes Memoir

Mr. Thurston

Employment

VI

The Treatise was no failure in any ordinary sense of the word. Nor was it a mere succès d'estime: everybody saw its points and, whatever his qualifications, paid respects to Keynes's great effort. Even damaging criticism, such as Professor Hansen's criticism of the fundamental Equations[1], or Professor von Hayek's criticism of Keynes's basic theoretical structure[2] were accompanied with a well-deserved eulogy. But from Keynes's own standpoint it was a failure and not only because its readers did not measure up to his standard of success. He had somehow missed fire – it had not really made a mark. And the reason was not far to seek: he had failed to convey the essence of his own personal message. He had written a treatise and, for the sake of systematic completeness, overburdened his text with material about price indices, the modus operandi of banks, deposit creation, gold and what not that, whatever its merits, was alien to current doctrine and hence, for his purpose

1) Alvin H. Hansen, A Fundamental Error in Keynes's Treatise on Money, this Review 1930, and Hansen and Tout, Investment and Saving in Business Cycle Theory, Econometrica 1933.

2) F.A. von Hayek, Reflections on the Pure Theory of Money of Mr Keynes, I and II, Economica 1931 and 1932. Hayek went so far as to speak of an "enormous advance". Nevertheless Keynes replied not without irritation. As he himself remarked on another occasion, authors are difficult to please.

~~merits, and little or nothing to what he really was anxious to say. However, systematic employment implies the use of models, and the stuff about price level, the modes operandi of bankrate, deposit creation, and the like, that was current doctrine at least, was not adequate to carry out Keynes's purpose and sufficiently protective.~~ He had entangled himself in the models of an apparatus that broke down each time he attempted ~~tried~~ to make it grind out his own meanings. There could have been no point in trying to improve the ~~thing~~ work in ~~the light of~~ details. There could have been no point in trying to ~~fight~~ criticisms the justice of many of which he ~~had to have~~ had to admit. There was nothing for it but to abandon the whole ~~thing~~, hull and cargo, and to start afresh, to renounce allegiances ~~which~~ he was quick to learn the lessons.

Resolutely ~~retiring~~ cutting himself off from the derelict, he braced himself for another effort, the greatest of his life. With brilliant energy he took hold of the essentials of his message and bent his mind to the task of forging a conceptual apparatus that would express these and – as nearly as possible – nothing else. He succeeded to his satisfaction, ~~after~~ but ~~soon~~ soon as he had done so, in December 1935, he buckled on his new armour, unsheathed his sword, and ~~attacked~~ took the field again, boldly claiming that he was going to clear economists out of the ~~the~~ ruts of 150 years' standing and into the promised land of truth.

Hansen, Alvin H. Memoirs on John M. Keynes

Those around him were fascinated. While Keynes was ~~recreating his~~ remodelling his thought, he currently talked about it in his lectures, in conversation, in that "Seminar" that used to meet in his rooms at King's. And there was a lively give and take. "... I have depended on the constant advice and constructive criticism of Mr R. F. Kahn. There is a great deal in this book which would not have taken the shape it has except at his suggestion" (General Theory, Preface, p. VIII) Considering all the implications of Richard Kahn's article on The Relation of Home Investment to Unemployment, published in the Economic Journal as early as June 1931, we shall certainly not regard ~~[illegible]~~ those two sentences of overstatement. Some credit was also given, (in the same place) to Mrs Robinson, Mr Hawtrey and Mr Harrod +). There were others – (some) of the most

+) Mr Hawtrey's relation to the book can never have been any other than that of an understanding and, up to a point, sympathetic critic ~~in his own right~~. He never was, of course, a Keynesian. From the Tract to the Treatise, Keynes was a Hawtreyan. Mr Harrod may have been moving independently towards a goal ~~not far from~~ that of Keynes, though he unselfishly joined the latter's standard after it had been raised. Justice imposes this remark. For that eminent economist is in some danger of losing the place in the history of economics that is ~~this~~ by right, both in respect to Keynesianism and in respect to Imperfect ~~(or Monopolistic)~~ Competition. Not less do I feel bound to advert to Mrs Robinson's claims. It is highly revelatory of the attitude of the academic mind to women that she was excluded from the above mentioned seminar (at least she was not invited on the occ →

footnote joke on

occasion which I addressed it). But she was in the midst of things. Proof of this are her Parallel on Saving and Investment (Economica, February 1933) which article was a most skilfully fought rearguard action covering retreat from the Treatise; and, still more significant of her role in the evolution of the General Theory, her Theory of Money and the Analysis of Output, published in Economic Studies (as early as October 1933, in the Review of Economic Studies.

Memoir on John M. Keynes

Cambridge

promising young men among them. And they all talked.
Glimpses of the new light began to caught by individuals
all over the Empire and in the United States. Students were thrilled.
A rare of anticipatory enthusiasm swept the world so far as
inhabited by economists. ~~Yet Harvard students felt~~ (From the bookcases at last, Harvard
students felt unable to wait until it could be available
at the bookstores: they clubbed together in order to speed
up the process and to arrange for direct shipment
of a first parcel of copies.

Success was instantaneous and, as we know, sustained.
Unfavorable reviews of which there were many only helped. A
Keynesian school ~~sprang into~~ formed itself, not a school in that
loose sense in which some historians of economics speak of a
French, German, Italian school but ~~one in the sense~~ a genuine
one which is a quasi-religious entity ~~and~~ namely a group ~~one~~ that ~~has~~ professes allegiance to
Masters and One Doctrine, and has its inner circle, its
propagandists, its watchwords, its esoteric and its popular doctrine. Nor is this all. Beyond the pale
of orthodox Keynesianism there is a broad fringe of sympathizers
and beyond this again are the many who, whether doubtful, in one form or another,
readily or grudgingly, ~~have absorbed~~ some of the spirit or individual items of Keynesian analysis. There are but two ~~similar~~ analogous
cases in the whole history of economics – the Physiocrats and
the Marxists.

This in itself is a great achievement that claims admiring recognition
from friends and foes alike and, in particular, from every teacher

from Alexander Memoir on John M. Keynes

Memoir on John M. Keynes

who experiences the ~~unifying~~ enlivening influence in his classes.

~~Still applying to readers who might feel that this article calls for apology let me illustrate the impact of Keynes upon students by the following analogy: Fanny's First Play, Bernard Shaw's, in the best Shavian style, introduces his own name into a conversation. So soon as it is mentioned the company opposite stares as seen to bring once with potential displeasure, and they all stare off with one voice and raised forefingers: "Shaw?" — and then stop and look blankly at each other. To call this exactly the kind of thing that happens in a company of young economists when someone mentions the name Keynes.~~

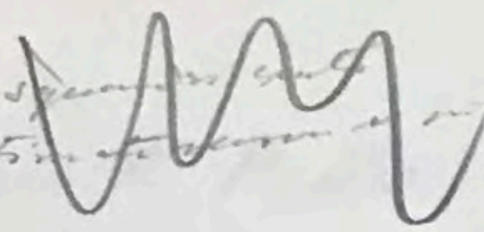
There cannot be any doubt, unfortunately, that in economics such enthusiasms and correspondingly strong aversions — never flare up unless the cold steel of analysis delineates a temperature not naturally its own from the real or putative political implications of the analyst's message. At no rate glance at the ideological bearings of the book. Most orthodox Keynesians are "radicals" in one sense or another. The man who wrote the essay on the Villiers Connection was not a radical in any ordinary sense of the word. What is there in his book that "pleases them?" ← → In an excellent article in this Review Professor Wright [+] has gone so far as to say (~~p. 287~~) that "a conservative candidate could conduct a political campaign largely on quotations from the General Theory." True, but true only if this →

[+] D. McC. Wright, The Future of Keynesian Economics, American Economic Review, June 1945, p. 287. This article, in spite of some differences of opinion, usefully complements my own in many points but consideration of space forbid me to enter.

Footnote + ¶ to preceding page

H) This is why there is not ample room for that turn of phrase that occurs so often in the Keynesian literature: "Keynes did not really say this" or "Keynes did not really deny that". In the General Theory most of the explicit qualifications occur in chapters 18 and 19. But the only possible reference to all the implicit ones is passim. (the logic of the deterministic system is not really impugned (p. 378).) ~~Stat~~ Even Say's law (~~the law of the market~~ in the sense defined on p. 26) is not completely thrown out; even the (the existence of a mechanism that tends to) equilibrating ~~effect on~~ saving and investment decisions ~~of the rate of interest~~ — and the role of interest rate in this mechanism — (and even the possibility that a reduction of money wages may eliminate an output gap) is not absolutely denied; though, to be sure, only in application to very special cases, ~~only~~, the validity of the first and the existence of the other two are occasionally recognized. (Critics are therefore in constant danger of being ~~Therefore if many critics should happen~~ ~~such statements as, for instance, that Keynes's theory amounts to saying that if the equations were autocapital and that to the causes destroys it, they would at once stand~~ convicted of "gross misrepresentation" exactly as many critics of Malthus first Essay invariably ran into a ~~fire~~ volley of quotations from the 2nd edition — in which in fact Malthus went far towards explaining away Malthusianism. But it is impossible to go into all this here. ~~One point only should not go unmentioned. It requires no elaborate argument to convince us that the economic engine will stall — and need monetary injections — if all its ~~dy~~ organs of adjustment especially commodity prices, wage rates and interest rates are paralyzed by ~~assumption~~.~~ In the article quoted, Professor Knight offers instructive examples.

Hansen Memoir on John M. Keynes



candidate knows how to use asides and qualifications. Keynes was no doubt far too able an advocate ever to deny the obvious. To some extent, though probably to a small extent only, his success is precisely due to the fact that even in his boldest strokes he never left his flanks quite unguarded — as many critics of either his policies or his theories are apt to discover to their costs +) Disciples do not

+) footnote on next page

look at qualifications ~~or at any of the items in Professor Knight's lengthy~~ They see one thing only — an indictment of private thrift and the implications this indictment carries with respect to the Managed Economy and Inequality of Incomes. In order to appreciate what this means ~~it is necessary to recall to mind of all readers,~~ it is necessary to recall that, as a result of a long doctrinal development, Saving had come to be regarded as the last pillar of the bourgeois order. In fact, old Adam Smith had already disposed pretty much of every other: if we analyze his argument closely, — I am speaking, of course, only of the ideological aspects of his system — it amounts to an all-round vituperation directed against "slothful" landlords and grasping merchants or "masters" plus the famous eulogy of Parsimony. And this remained the keynote of most non-Marxist economic ideology until Keynes. Marshall and Pigou were in this boat. They, especially the latter, took it for granted that inequality or some actual degree of inequality was "indesirable". But they stopped short of →

7

attack upon the Pillar. ~~The~~ Most men who entered the field in the 20s and 30s had renounced allegiance to the bourgeois theme of life, the bourgeois theme of values. Many of them sneered at the ~~economic motive, the~~ profit motive ~~motive~~ and at the element of personal performance in the capitalist process. But so far as they did not embrace straight socialism, they still had to pay respect to Saving (offsetting or reserve) under penalty of losing caste in their own eyes and ranging themselves with what Keynes so tellingly called the economists' "underworld". But Keynes broke their fetters: here, at last, was a theoretical doctrine that not only obliterated the personal element and was, if not mechanistic itself, at least mechanizable, but also smeared the pillars with dust; a doctrine that may not actually say, but can easily be made to say, both that "who tries to save destroys real capital" and that, via saving, "the unequal distribution of income is the ultimate cause of unemployment."+) This is what the Keynesian Revolution amounts to. And, thus defined,

+) And, after all, a glance on pp 372-3 and 376 of the General Theory will convince anyone that Keynes actually came pretty near to authorizing both statements. ~~For~~ One must be as punctiliously conscientious as is Professor ~~Hight~~ Wright in order to say that he did not actually do so.

the phrase is not inappropriate. And this, and only this, explains and, to some extent, justifies Keynes's change of attitude towards Marshall which is neither understandable nor justifiable upon any scientific ground. Socialists may "smile disdain" at the performance

→

→ But they are strong. Much more personal force (and ingenuity are) needed in order to blow up a dogma (– to the satisfaction of any considerable number of people –) from within the ideology of which it is a part than are needed in order to blow up that ideology itself.

~~There is something that should not go unmentioned.~~ But quite apart from the precious gift that Keynes bestowed upon the man who craves for a rationalization of his anticapitalist will and yet does not wish to declare for straight socialism or fascism, there is another gift that is not less valuable to a great many economists. Before the Keynesian era, economics was growing increasingly complex and economists felt to be drowning in ever more formidable masses of facts and freezing among ever more intricate refinements of theory. Many felt losing their ability and, ~~this~~ this was worse, even those who did not, had to confess their inability to produce simple results that could be readily turned into practical recommendations. The General Theory changed all that: a few variables instead of a few relations instead of a mage of them. (a Milky Way,) but simple results galore! The times had returned of Mrs Marcet and Mrs Trimmer – one more governess could teach her wards how to manage the economies of nations and how to solve "real problems." But – and this is the decisive point – exactly as it is the case of the Ricardian economics, there was in addition enough to attract, to inspire even, the sophisticated. The same system that looked up so well in the ancient notions of the untutored mind, proved satisfactory to the best brains of the rising generation of theorists. "Some

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of them felt – still feel for all I know – that all other work in "theory" could and should be scrapped. But even those who did not feel like this ~~put the former fault with many details~~, yet paid homage to the man who had given them a well defined model to handle, to criticize, and to improve – to the man whom they loved as they loved the fresh breeze from the sea, to the man who symbolized at least, though he may not actually have done, what they wanted to see done. The negative reaction of the majority of older men added precisely the fuel that was needed for the obvious interpretation they put upon the "Keynesian Revolution." ~~No doubt, this will not last. In fact this passing already. But~~ (In this situation, hostile criticism was powerless. Or rather, it was itself a kind of homage. ~~in~~ And in fact, as with Marx, it is possible to admire Keynes even though one may consider his Vision to be wholly wrong and everyone of his propositions (to be) misleading.

VII

The social Vision first revealed in the Economic Consequences of the Peace, the Vision of an economic process in which investment opportunity flags and saving habits nevertheless persist, is ~~completely~~ theoretically implemented in the General Theory of Employment, Interest, and Money (Preface dated December 13, 1935) by means of three (selected) concepts: the consumption function, the efficiency-of-capital function, and the liquidity-preference (function) +).

+) Distinctive terminology helps to drive home the points an author wishes to make and to focus his readers' attention. This (though nothing else) justifies the re-naming of Irving Fisher's marginal rate of return over cost — of the priority of which Keynes fully recognized — and also the use of the phrase, liquidity preference, instead of the usual one, hoarding. Consumption function is certainly a better shell for Keynes's meaning than the Malthusian phrase, Effective Demand, which he also used, for nothing but confusion can come from using the concepts of Demand and Supply outside of the domain (partial analysis) in which they carry rigorously definable meaning. — It is not without interest to note that Keynes called his assumptions about the forms of the consumption and liquidity-preference functions Psychological Laws. This was of course another Emphasizing Device. But no tenable meaning can be attached to it, not even so much meaning as attaches to the "law" of satiable wants." In this as in some other respects, Keynes was distinctly old-fashioned.

→ These together with the given wage-unit and the equally given quantity of money "determine" income and, ipso facto, ~~employment~~ (if and so far as the latter is proportional to the former), the great independent variables to be "explained." What a cordon bleu to make such a sauce out of such scanty material! →

+) It is ~~[illegible]~~ really an injustice to Keynes's achievement to reduce it to the bare bones of its logical structure and then to reason on these bones as if they were all. Nevertheless great interest attaches to the attempts that have been been made to cast his system into exact form. →

footnote continues

It is neither necessary nor possible to describe the analytic scheme itself but will attempt to sketch in a few words the main features of it. Among the many renderings of it there are of particular interest that make the attempt to cast it into an exact form. (H.D. Reddaway's review in the Economic Record 1936)

I want in particular to mention: R. F. Harrod's Mr Keynes and Traditional Theory Econometrica, January 1937; J. E. Meade, A Simplified Model of Mr Keynes' System, Rev. of Economic Studies, February 1937; J. R. Hicks, Mr Keynes and the "Classics", Econometrica April 1937; O. Lange, The Rate of Interest and the Optimum Propensity to Consume, Economica February 1938; P.A. Samuelson, The Stability of Equilibrium, Econometrica, April 1941 (with dynamical reformulation); and A. Smithies, Process Analysis and Equilibrium Analysis, Econometrica January 1942 (also a study in the dynamics of the Keynesian model).

~~It is interesting to note that, with the exception of the first two papers mentioned, these investigations~~ In the hands of writers less in sympathy with the spirit of Keynesian economics some of the results presented in these papers might have be turned into serious criticisms. This is still more true of F. Modigliani, Liquidity Preference and the Theory of Interest and of Money. Econometrica, January 1944.

~~be just neglected in the necessary or by strictly output - or employment~~ ~~and in the Keynesian system practically mean the same thing, — is determined by means of the~~

Let us see how he did it.

(1) ~~Of~~, the first condition for simplicity of a model is of course simplicity of the vision which it is to implement. ~~Keynes's Vision fulfilled the condition to the point of his simplification theories to depart its purpose.~~

And simplicity of Vision is in part a matter of one's genius and in part a matter of one's willingness to pay the price in terms of the factors that have to be left out of the picture. But ~~if~~ we 'place' ourselves on the standpoint of Keynesian orthodoxy and choose to accept his vision of the economic process of one age as the gift of genius ~~that was the simple~~ whose glance pierced through the veils of the simple essentials that lie behind the surface phenomena, then there can be little objection to ~~the~~ of principle ~~fewness of his variables and only admiration for the rectangle~~ of his Aggregative Analysis that produced his results. Since the "aggregates" chosen for variables are, with the exception of employment, monetary quantities or expressions, we may also speak of Monetary Analysis and, since National Income is the central variable, of Income Analysis.

Let us see how he did it.

~~He used the~~ By reducing, as we have just seen, ~~called~~ the Milky Way of economic variables to a few and thus resolutely adopting the ~~method of~~ Aggregative Approach. Since the aggregates chosen for variables ~~[illegible]~~ are, ~~made~~ with the exception of employment, monetary quantities or expressions we may also call his analysis Monetary Analysis, and since the central aggregate is national income, Income Analysis. Of course he paid the price. Aggregative analysis can only deal with those phenomena — and causal factors — that are visible in the aggregates: ~~and all others [illegible]~~ like a telescope, it makes us see certain things very clearly and others not at all.

No new paragraph

Richard Cantillon was the first, I think, to indicate ~~sub~~ a fully-fledged schema of aggregative, monetary, and income analysis, the one worked out by François Quesnay in his tableau économique. Quesnay, then, is the true predecessor of Keynes, and it is interesting to note that ~~Keynes's [illegible]~~ his views on saving were ~~attitude [illegible] strikingly~~ identical with those of Keynes: the reader can easily satisfy himself of this by looking up the Maximes. It should however be added that, in this respect, the General Theory does not stand alone in modern literature: it is but the great success in a family that had been rapidly growing before.[1]

[1] The quickest way to learn how far aggregative analysis had progressed before the publication of the General Theory is to read Tinbergen's survey article in Econometrica, July 1935.

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Keynes further simplified his structure

(2) By avoiding, as much as possible, all complications that arise in Process analysis. The exact skeleton of Keynes's system belongs, to use the terms due to Ragnar Frisch, to Macrostatics not to Macrodynamics. In part this limitation must be attributed to the formulators of his teaching rather than to his teaching itself which contains several dynamic elements, expectations in particular. But it is true that he had an aversion to "periods" and that he concentrated attention upon considerations of static equilibrium. This removed an important barrier to success — a difference equation as yet acts upon economists like the face of Medusa.

(3) By confining (Furthermore, he confined) his model (—though not always his argument—) strictly to the range of short-run phenomena. While points (1) and (2) are commonly emphasized it does not seem to be realized sufficiently how very strictly short-run his model is and how important this fact is for the whole structure and all the results of the General Theory. The pivotal restriction is that not only production functions and not only methods of production but also the quantity and quality of plant and equipment are not allowed to change, a restriction which Keynes never tires of impressing upon the reader (at crucial turns of his key) (see, e.g. p. 245 and p. 114) +)

+) Strictly, some change in the quantity of equipment must be admitted. But it is conceived of as so small, at any given point of time, that its effect upon the existing industrial structure and its output can be neglected.

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approximately

This permits many otherwise impossible simplifications, for instance it permits to treat employment as proportional to income or output, so that the one is determined in terms of time

so soon as the latter is, ~~but~~ limits applicability of his analysis, to a few years at most – perhaps the ~~light~~ duration of the "Kuznets cycle" – and in terms of phenomena, to the factors that would govern the greater or smaller utilization of an industrial apparatus if so ~~large~~ the latter were assumed unchanged. All the phenomena incident to the creation and change in this apparatus, that is to say the phenomena that dominate the capitalist process are thus excluded from consideration. As a picture of reality this ~~construction~~ model becomes most nearly justifiable in periods of depression when also liquidity preference comes nearest to being an operative factor in its own right. Professor Hicks was therefore ~~right~~ correct in calling Keynes's economics the economics of depression. But from Keynes's own standpoint, his model derives additional justification from the secular-stagnation thesis. Though it remains true that he tried to implement an essentially long-run vision by a short-run model, he secured, to some extent, the freedom for doing so.

~~By~~ By reasoning (almost) exclusively about a stationary process or, at all events, a process that stays above oscillates about, levels of ~~stationary~~ full-employment equilibrium is the ceiling. With Marx, capitalist evolution issues into breakdown. With J.S. Mill, it issues into a stationary state that works without hitches. With Keynes, it issues into a stationary state that constantly threatens to flop. In a sense, Keynes may be said to teach a "breakdown theory". Though it's quite different from Marx's, it has an important feature ~~has its~~ in common with the latter:

in both theories, the breakdown is motivated by causes inherent to the working of the economic engine not by the action ~~of~~ by ~~factors~~ factors external to it. This feature naturally qualifies Keynes's theory well for the role of "action-dizer" of anti-capitalist solution ~~and suggests a need either~~

+ (4) Quite consciously, Keynes refused to go beyond the ~~factors~~ factors that are the immediate determinants of income (and employment) & the himself recognized freely that these immediate determinants (which may "sometimes" be regarded as "ultimate independent variables") "must be capable of being subjected to further analysis, and are not, so to speak, our ultimate atomic independent elements" (p 247). This turn of phrase seems to suggest no more than that economic aggregates derive their meaning from the component "atoms". But there is more to it than this. We can of course greatly simplify our picture of the world and arrive at very simple propositions if we are content with arguments of the form: given A, B, C..., then D will depend upon E. If A, B, C... are things external to the field under investigation, there is no more to be said. If they are part of the phenomena to be explained, then the resulting propositions about what determines what may easily be mere understable ones acquire the semblance of novelty without meaning very much. This is what Professor Hicks has called Implicit Theorizing. +) But for Keynes, as for →

+) cp. his Italy article under that title in the Quarterly Journal of Economics vol 51, pp 337–51.

for A B C, the

[illegible]

→ Ricardo +) arguments of this type were but emphasizing devices:

+) The intellectual affinity of Keynes with Ricardo merits to be noticed. Their methods of reasoning are closely similar, a fact that has been obscured by ~~the differences in the results it induced Keynes to take as affinity between himself and Malthus that [illegible] of Keynes's admiration for Malthus's anti-saving attitude and by his evaporated dislike for Ricardo's teaching.~~

they served to single out and by so doing to emphasize a particular relation they thought important. Ricardo did not say: "Under present English conditions ~~in England~~, as I see them, free trade in foodstuffs and raw materials will, everything considered, tend to raise the rate of profit." Instead he said: "The rate of profit depends upon the price of wheat."

(5) Forceful emphasis on a small number of points that seemed to Keynes to be both important and inadequately appreciated being the Keynote of the General Theory, we find other emphasizing devices besides the one just mentioned. ~~Two~~ We have noticed already.+ Another is what writers are bound

+) See above, p. ... n.

to call overstatements, overstatements moreover which cannot be reduced to defined level, because results precisely depend upon the excess. But it must be remembered ~~that~~, not only that, from Keynes's standpoint these overstatements were little more than means to abstract from

Either compact [illegible] fruit knife [illegible]

non-essentials, but also ~~that~~ the blame for them lies at our own door: we, as a body, simply will not listen unless a point be hammered in with one-sided energy. Granting, ~~then~~, for the sake of argument, that the points in question are actually important enough to merit being hammered in, and remembering that the gems of unqualified overstatement do not occur in the General Theory itself but in the writings of some of Keynes's followers, we still appreciate this method of flavoring what I have described as the Sauce.

Three examples must suffice. First, every economist knows – if he did not he could not help learning it from conversation with businessmen – that any sufficiently general change in money wage rates will influence prices in the same direction. Nevertheless it is not the practice of economists to take account of this in the ~~general~~ theory of wages. Second, every economist should have known that the Forget-Smith – J. S. Mill theory of the saving and investment mechanism was inadequate, and that, in particular, saving and investment decisions were too closely linked together. Yet, if Keynes ~~and have~~ presented a properly qualified statement of their true relation, would he have elicited more from us than a mumble to the effect: "Yes... that's so ... of some importance in certain cyclical situations... what of it?". Third, let any reader look up pp. 165-6 of the General Theory – the first two pages of Chapter 13, on the "General Theory of Interest." What will he find? He will find that the theory, according to which the investment demand for savings and the supply of savings that is governed by time-preference ("which I have called the propensity to consume") is equated by the rate of interest "bears down" because "it is impossible to deduce the rate of interest →

→ merely from a knowledge of these two factors". Why is this impossible? Because the decision to save does not necessarily imply the decision to invest: we must take account of the ~~fact~~ possibility that the latter does not follow, or not follow promptly.* I will lay any odds that this perfectly reasonable proposition in the tenor of current teaching would not have greatly impressed us had he left the matter at this. It led to be Liquidity Preference to the peg — and interest nothing but the reward for parting with money — and so on in a well-known sequence (this cannot be over the storing of his own theory) in order to make us sit up. And it was made to sit up to some purpose. For many more of us will now listen to the proposition that interest is a purely monetary phenomenon than were ready to listen 35 years ago.

Insert the following page

(6). It seems evident that Keynes wished to secure his major results without appeal to the element of Rigidity just as he spurned the aid he might have derived from imperfections of competition.+) There were points however at which he was unable to do so, especially the point at which the rate of interest became rigid in the downward direction because the interest-elasticity of the Liquidity Preference demand for money became infinite. And at other points, rigidities stood in reserve, to be appealed to in case the front-line argument failed to convince. It is of course always possible to show that the economic apparatus will fail to function if a sufficient number of its vital organs are paralysed. Keynesians will not have to contest with this Ross result any other theorists. But it is something to be able to show,

+) The latter factor was however inserted by Mr Harrod.

This is to be inserted, in indicated place on preceding page, as a special paragraph.

But there is one word in the lines that cannot be defended on these lines – the word General. These emphasizing devices – even if quite unexceptionable in other respects – cannot do more than indicate very special cases. ~~Keynes and his followers~~ Keynesians may hold that these special cases are the actual ones of our age. They cannot hold ~~that~~ more than that.+)

+) This has first been pointed out by O. Lange, O.C., who also paid due respect to the only truly general theory ever written – the theory of Léon Walras, the neatly stowed ~~to extract Keynes's as special case.~~

that the latter covers Keynes's as a special case.

~~→ [illegible] that the necessary conditions for different norms.~~
~~come to similar conclusions~~ to show that the economic system will cease to work if a sufficient number of its adaptive organs are paralyzed. Keynesians like this fire escape no more than do other theorists. Nevertheless it is not without importance. +) The classical example is equilibrium under employment →

+) I have sometimes wondered why Keynes attached so much importance to proving that there may — and under his assumptions generally will — be less than full employment in perfect equilibrium of perfect competition. For there is ample supply of verifiable explanatory factors to account for the actual unemployment we observe at any time. ~~There is of course not the slightest foundation for his assertion that the man of straw whom he called the "classical" economist ever held that~~ Not only the theorist's ambition can induce us to risk for more. ~~Keynes's assertion that the straw man whom he called "classical economist" [illegible]~~ The question of the presence of involuntary unemployment in perfect equilibrium of perfect competition, a state that even the straw man whom Keynes called "classical economist" never believed in as a reality, is no doubt of great theoretical interest. But practically, Keynes should have faced equally well with the unemployment that may exist in a permanent state of disequilibrium. As it is he clearly failed to prove his case. But inflexibility of wages in the downward direction stands ready to lend it aid. — The theoretical question itself is the subject of a discussion that suffers from the failure of participants to distinguish between the various theoretical issues involved. But we cannot enter into this.

(7) ~~The~~ most finally advert to Keynes's brilliance ~~skill~~ in the forging of tools ~~that serve the purpose~~ of analysis. ~~The~~ tools, ~~adapted to the purpose of Kahn's Multiplier~~ for instance, at the ~~brilliant~~ skilful use made of Kahn's Multiplier or ~~*~~ at the felicitous creation of the concept of User Cost which is so helpful in defining (his) income and may well be recorded as a novelty of some importance. What I admire most in these and other conceptual arrangements of his, is their adequacy: they fit his purpose as a well-tailored coat fits the customer's body. Of course, precisely because of this, they possess but limited usefulness irrespective of Keynes's peculiar aims. A fruit knife is an excellent instrument for peeling a pear. The chef who uses it to attack a steak has only himself to blame for unsatisfactory results.

Mrs Roosevelt

New paragraph: the sentences between the brackets are to form the last paragraph.

VIII

At this I will leave it. I am not going to grade the General Theory as if it were a student's exam. book. Moreover I do not believe in grading economists — the men whose names one might think of for comparison are too different, too incommensurable. Nor am I going to prophesy how future generations will deal with his teaching. [Whatever happens to his works the memory of the man will live — with both Keynesianism and the reaction to it.]

Everyone knows the stupendous fight the valiant warrior put up for the work that was to be his last. Everyone knows that during the war he entered the Treasury again and that his influence grew along with that of Churchill, until nobody thought of challenging it. ~~Also of the~~ Everyone knows of the honor that has been conferred upon the House of Lords, but, of course, of Bretton Woods and the English loan. These things are for some scholarly biographer to worry about who has all the materials at his disposal.

Schumpeter

These are notes taken by a student at the lecture Schumpeter gave at the Institute of World Affairs at Taconic last summer. So far as I know this lecture represents the fullest exposition of his ideas on capitalism. I therefore thought they were worth circulating.

Arthur Smithies

Capitalism in the Postwar World 1-20

Institute of World Affairs. Hadden House Library, August 29, 1949.
Twin Lakes, Connecticut. # 3:30P.M.

Lecture by Professor Joseph A. Schumpeter, Harvard University

CAPITALISM, SOCIALISM AND DEMOCRACY.

This lecture will deal with economic sociology, especially with the problems of the public servant behind the frame of the social background. All problems are set by (a) the objective conditions, and (b) the attitude we take toward them. The attitudes are determined by the kind of people the deciding agents are. What kind of people the deciding agents may be is dependent on the national cultures they come from; i.e., on their previous social organization. I say this because then the problems are (1) easier to understand, and (2) they are set up in the form Karl Marx set them. When tribes have conflicting interests, look at the kind of people they are for the reason. People behave differently in different situations; there is no form of universal rational man. Feudal society had a characteristic way of dealing with group problems that arose— its similarities with other comparable economically organized societies don't explain everything about the culture, but they do explain much. Karl Marx's line is a great contribution to our understanding of society. He developed a theory of foreign relations of capitalist society. His followers who have developed it are (a) Otto Bauer, (b) Rudolf Hilferding, and (c) Leon Trotsky.

Let us examine Trotsky. He puts forth the proposition that

imperialism is the last stage of capitalist society. Imperialism here is a characteristic attitude of one capitalist nation toward another. This complements the proposition that imperialist wars will be turned into civil wars; capitalist society breaks down in order that the socialist phoenix may arise. The theory has been badly damaged; the preconditions that capitalist society should develop into imperialist society have not come true. I advance the proposition that not imperialism, but laborism is the last stage of capitalism. Laborism signifies here that capitalist society at that stage is the capitalist society in which the labor interest is predominant. Marx would have thought this impossible, but this is not a criticism of Marx. So far as this goes, the Marxist ideas are not correct, but this admission does not damage the Marxist argument materially. The end will result in socialism easier than the imperialist state might have done.

To illustrate this, take the United Kingdom as an example. I will apply the idea to foreign relations after this short analysis. Marx would never have argued as he did if he saw society running towards that of a labor or a farm society. In the laborist society, other interest groups count only insofar as they serve indirectly labor interests. For example, note the present advertising motifs: manufacturers call their interests as being indirectly beneficial to the working class. In art and science, this has killed the creed of the arts, "art for art's sake" and has substituted interest for the moral code. All arts are now applied, not pure. In physics and mathematics (I point out Hogben and others of his type), a utilitarian theory of "pure science" is being developed.

Capitalism in the Postwar World 1-20

Capitalists society in England ran into the interests of the working class. How far is this an arrangement that can last? We must first guard against sources of wrong diagnosis: bourgeois society had many feudal elements which protected its own interests. Other societies will do this too. Take, in England, the diplomatic tradition: ancestrally trained people hold these positions and serve what purposes are to be served, but in so doing they modify these purposes. So laborism is a form of society that predominates in England today, but not completely. Therefore we have many side developments to expect. I wish to add a footnote to elaborate my point. (1) What else can we say? As economists, we can say that the labor interest in the labor market is still short of dominating importance, because (a) labor can't insist on the clause of "all or none," i.e., labor wants higher wages, but as yet can't determine who or how many workers will be hired. (b) There still exists the right of the manufacturer to fix prices and raise these if he has to raise wages—therefore wage increases can be turned into inflation. So the labor market is not completely dominated by labor. There is as yet an indeterminate bilateral exchange; labor domination is complete only when employer interests are pressed to the marginal cost curve. (2) What will happen when these shortcomings have been eliminated and labor does what it wants? (a) Prices will be reduced to prime costs; i.e., society will not renew fixed costs and capital. (b) Only if the government borrows at a low rate of interest could it maintain the status quo for a while. (c) Government spending and subsidy: as this goes on we find that the system of private investment will be sabotaged and the way for socialism will be prepared. This is better (in the sense that it entails

hardship) than the transitory stage of Marx, which paralyzes all activity. Please keep this footnote in mind in the interpretation of my later remarks.

In the laborist society, the labor market is run from the aspect of labor interest. But government taxation and expenditures must also be taken into account. Because of this fact, the bourgeoisie also never had a complete hold of society. Feudal finance principles: taxation was to be undertaken for maximum revenue in order that it might be spent by the ruling elite (lords, court, etc.). Now we have the same thing in a laborist society; the social system is exploited for a class purpose; it is not a societal purpose as a whole. The working class has replaced Mme. du Barry, and we have the inverse of the feudal system. This is just analysis, not any value judgment on my part.

The laborist society has these characteristic features; (1) labor market control, (2) capital market control ("cheap money"), (3) public finance has a purpose in the budgets of laborist states. Greater sums are spent for food subsidies than for defense, and the working class has the luxury of services which include the famous gratis wigs of England. The American worker is taxed to pay for these services. As a result of foreign policy, this is a fabulous work of art. It is a brilliant performance by the best politicans and bureaucrats the world has yet produced.

I wish to present now the characteristics in foreign policy taken from the background of the laborist state. These are not inclusive; we can only say what the probable course of events will be, for there are indeterminate factors; e.g., the threat of communist Russia which will react on the laborist state. England

as a laborist state is dangerous for it is bankrupt; it can't pay its own way as a nation. It can't build up an army from its own means, for then it would have to decrease its social subsidies and services. This contradicts the aims of the laboring class. As the English political class established itself as the exponent of bourgeois interests, so it has now established itself as the exponent of the labor class. For labor, there has been a rising real wage and a decreasing of hours of work without serious sacrifices. Only the labor interest counts. This is a success of the labor government, not a failure. (I wish to insert a second footnote: on the subject of rising real wages for the working class, one is apt to think of the rationing system and the price indices to explain the opposite. These are not reliable on this score.) The labor government has been successful in realizing its own aims, but there has been little renewal of industrial operators and armament. This is characteristic; for the labor mind, its interests are not to be retracted. The situation is dangerous for us.

Russia is not a laborist state; it is a dictatorship. The same analysis does not hold for it. We can't act as either of the two; our foreign policy is domestic policy in that it has to founder on various lobbies.

The situation of the laborist state in the face of a dictatorial power is dangerous and uncomfortable. But let us disregard this element for the moment and consider laborism as a principle. We said it eats up armament and capitalization costs. Why can't they capitalize? This is the reason: the dominant interest (i.e., the labor class) doesn't want eternal economic progress. Take the dictum of Keynes, "in the long run, we shall all be dead" —if you accept this, why build for the future? And if national

future has no meaning, the Havana Charter and the multi-lateral trade agreements seem to have no meaning either. In re the trade agreements: if we have only a world of laborist states, working for the interests of the labor class, each country will need certain imports for certain exports. This implies a schema of willingness to import and export, cf. the Frisch method. But how can these items be made to fit? The laborist world would not have the phenomenon of economic progress, but it would be perfectly workable for the rest. Objective problems are one thing; attitudes toward them are another; if you don't want progress, you don't want it. The laborist society has a ruling group too, and their attitudes are important. Democracy, however, will be muzzled in this process.

What are the possibilities? They click with certain 19th Century ideas. They result in abstract interests. Such a situation is dangerous in the face of a military dictatorial power. Military power is especially effective in such a situation.

Finis. Question and answer session.

Prof. Smithies. Harvard: How complete is your explanation of the present foreign policy? It certainly explains the demand for American assistance to others, but why should we give this money? The laborist states live in inflation, so they must have complete control of foreign trade. If so, (a) why does the United Kingdom feel so tender toward its empire? (b) and why does the United States accede to the laborist demands?

Schumpeter: I must give an apology for my schema. It explains the Marxist schema, but it is too brief as here presented to explain its shortcomings. But I have not left out the qualifications: (a) laborism is not "pure" at the present; the latter analysis

does not hold until the system is complete. The UK can see its overall interests in places like India; the policy elite is still thinking in terms of the empire and its own, rather than just the labor class's, interests. (b) We still have a tendency to carry over our admiration and respect for England. This is not now justified, but we respect England. The things we attribute to her policy have in fact nothing to do with it. To cite another example: were the results of the recent Italian election due to Hoffman? No, they were the results of the activity of the Catholic Church. When Italy was founded (1859-66 and 1871), the regimes were set up on the French model. Italy had a Gladstonian liberal period in which some of the intellectuals but never the masses were hostile to the Catholic Church. These intellectuals had some laws passed against the Church: the Catholics resented it, and the supporters of liberalism got fewer and fewer votes. One may note the same thing in Mexico.

Prof. W. Y. Elliott, Harvard: Methodological simplicity is a valuable tool, Joe, but the laborist state, as you call it, came into being against a background of repudiation of Marxism. Admittedly, this school has economics as its primary factor. But as to the structure of laborism, has the labor class all this class solidarity? I'd question that point. And does the welfare state mean the same thing as a laborist state? Schumpeter: No. Elliott: I've always felt that the causes of a lot of this could be rooted in the acceptance of universal suffrage. To get back to my point; while democracies will not generally plan for the future if it conflicts with short run interests, they have shown they can do it if they are pressed. Do you contend that democracies are now so laborist that

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they are sterile? I don't think this country is in that stage yet. Your analysis doesn't take into account voluntary groupings which play a vital part in our national life. Laborism by your analysis (which puts economics in as the primary factor) seems to be an economic dterminism; maybe you've left out certain important elements. As I see it, the whole thing stands or falls on the point of class solidarity. If there are economic classes in the Marxist sense—and I'd argue this with you—then what you say is logical, if not complete; but if there are none, then the whole thing breaks down, and I think you have to admit that, Joe.

Schumpeter: Yes, I admit your points, but they don't affect the analysis. As I said, the analysis is not over-complete as presented here.

Elliott: But dammit, why should capitalist states have to go in the laborist direction? I can only see the issue of class-solidarity as deciding that, and so I ask you: do you assume economic classes in the Marxist sense?

Schumpeter: Hold it, Bill, I didn't say there was any determinism to laborism, but you're right, I do assume economic classes in leading into it, and my analysis hangs on that point. I think the facts have borne me out; England and Sweden are good examples for my thesis. There are no more rich people in England today. Britain is very far down the line to full laborism, so is Sweden. Sweden was able to pay its way, but that is because it was not involved in a war. Laborism can pay, but not unless it lives up to its maximum tax revenue. And circumstances may even force such a country to do so—then why the Marshall Aid? Strings are difficult to put on this aid. I think we ought to guarantee to

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defend England as such; it would be a lot cheaper. The English say they might go Communist, but there's no fear of that.

Stuart Collie, Yale: Could you elaborate your analysis of the nature of foreign trade under full laborism the world over?

Schumpeter: Laborism will eliminate higher incomes. Labor interests mean different things, however; an observer looking over the history of a generation might see labor interests as different from the labor interests as seen by a labor mind. With this in mind, we can say this: In the long run, things will balance out even in the laborist economy. The factors are (a) income from foreign investment and (b) the fact that exports are not the only commodities in trade, but that services (e.g., shipping, banking) also come into the account. There will be an all around multi-lateral arrangement of labor states in a static economy.

Notes taken by Peter K. Ogloblin,
1950, Harvard.
Ideologies Commission Chairman.

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The Place of the Communist Manifesto in the History of Sociology and Economics

Joseph A. Schumpeter

This paper is to appraise the position of the Communist Manifesto in the history of scientific sociology and economics and incidentally in Marx's own scientific work (Sections III and IV). Some of the necessary framework will be provided and some extrascientific aspects will be noticed first (Sections I and II). But I wish to emphasize at the outset that this paper is in no sense an essay in Marxology, that is, in what has by now become a special discipline of Marx the man and the thinker; and also that, but for an inevitable minimum, I shall neglect many of those things that readers might expect to find in a centenary appraisal. Very obviously the Manifesto was more than a piece of analysis. But it is as a piece of analysis that I am going to discuss it without any intention, if this need by added, of either debunking or glorifying it.

I

Friedrich Engels' Preface to S. Moore's English translation of the Manifesto, dated London, January 30, 1888, tells us all we need to know about the nature of the publication, the conditions under which it appeared, and its fortunes. Later research, including the work of the Marx-Engels Institute, has added a number of details and corrected others none of which, however, is of importance

1st Version of this article
Possibly part of History of Ec. Analysis

Article on the Communist Manifesto

The Place of the Communist Manifesto in the History of Economic Analysis

The purpose of this paper is to estimate--approximately--the position of the Communist Manifesto, first, in the history of scientific economics (III) and, second, in the evolution of Marx's scientific work (III and IV). This purpose is narrower than the purpose of a centenary appraisal of that document might be expected to be, and imposes neglect of many things that, from the standpoint of either Marxology or of political thought, might be considered as more important than what I mainly wish to say. Part at least of my readers may, however, see some justification in my trying to do that limited job. And some of the aspects to be neglected will not be entirely excluded. They will be noticed in order to provide a frame for my argument (I and II)

I

Friedrich Engels' Preface to S. Moore's English translation of the Manifesto, dated London, January 30, 1888, tells us all we need to know for our purpose about the nature of the publication, the conditions under which it appeared, and its fortunes. Later research, including the work of the Marx-Engels Institute, has added a number of details and corrected others none of which is of importance

to our purpose.* But Engel's Preface itself is important for us in several respects.

First, Engels made it quite clear that the pamphlet should not be called the manifesto of a communist party, for the communist group that "commissioned" Marx and Engels to write its "platform" did not amount to anything like what is usually meant by party. The Communist League, successor of the League of the Just, was a small group founded for purposes of education and propaganda that should not have been called a "workingmen's association" either, for both its original German membership and the allies it found later on in various western capitals of Europe consisted mainly of isolated individuals who were intellectuals rather than manual workers. The group, dissolved in 1852 (after the "Communist Trials" of Cologne) was numerically insignificant and is not known to have exerted any influence on the contents of the Manifesto. Viewed from the standpoint of the latter, it was hardly more than a "letterhead."

Second, Engels Preface explains why the classic document of modern socialism should have been called the Communist Manifesto. In 1847, so Engels told his readers, socialism had become a respectable middle class movement, i.e., it

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* We merely note, from Engel's Preface, that the Communist Manifesto was written, in German, in January, 1847, and "sent to the printer" (a small firm in London) in February; that the first French translation became available before June of the same year and the first English one (in G.J. Harney's Red Republican, London) in 1850; that the first American translation was published in the periodical of a brokerage firm—Woodhall and Claflin's Weekly; that a Russian translation (Bakunin's) appeared in 1970, another (Plekhanov's) in 1882. There were several translations into other languages before the end of the 1880's, i.e. before the German Social Democratic Party placed itself on Marxist ground. The authentic German edition of 1872 is of particular interest because of Marx's and Engels' joint Preface to it. No further data of this type are necessary in what is emphatically not an essay in Marxology.

had ceased to be a working class movement and revolutionary. Using a later expression, we may say that socialists--more correctly, some of them, had become "reformist." Still more important was it, as Marx and Engels rightly felt, to distance themselves from the various groups of "utopian" socialists that were then (1848) no longer taken seriously. Rather than risking to be mixed up with these they resolutely ranged themselves with the "crude, rough-hewn, purely instinctive communism" which they attributed to at least a portion of the working class. This resolve accounts for and in part excuses Marx's and Engel's failure to recognize doctrinal priorities of utopian writers in several important points.

Third, with admirable tact and feeling, Engels "considered himself bound to state that the fundamental proposition which forms its (the Manifesto's) nucleus,* belongs to Marx," while reserving his own claims to the extent that

* We shall deal with this "nucleus" at length (parts III and IV below), since it contains all that is of scientific interest in the Manifesto. But Engels' brief rendering of it (on p.6 of the International-Publishers edition) is strongly recommended to the reader's attention. Were it not for considerations of space I should quote it in full.

both he himself and Marx had been moving independently of each other toward that proposition for "some years before 1845"--perhaps since 1843. For this he offered his Condition of the Working Class in England in 1844 as evidence which there is no reason to refuse on the understanding that the undeniable difference between the two men in depth of comprehension and analytic power be appropriately balanced against the fact that in those years Engels was certainly farther along, as an economist, than was Marx.

Fourth, Engels was far from wishing to claim for the Manifesto any causal importance in the course of social history; in fact he could not have done so without contradicting the Marxist interpretation of history. But he claimed much too much for the First International (l.c. p.4) which "on its breaking up in 1874, left the workers quite different men from what it had found them in 1864." * And, on the lower level on which a Marxist is bound to keep when speaking of a mere document, Engels was the victim of a similar optical delusion as regards the Manifesto. For him, the Manifesto not only "reflects, to some extent, the history of the modern working-class movement" but also is "the common platform acknowledged by millions of workingmen from Liberia to California" (l.c. p.5). This must mean, if anything, that that history of the modern working-class movement is correctly interpreted by the fragmentary theory of the Manifesto—whereas it is quite clear that it is not because, not to mention other reasons, the increasing social and political weight of the working class has been a result of increasing real wages, per head, hence the consequence of a development the very possibility of which Marxism (especially in 1848) explicitly denied; and that the ideology of the proletariat, or a large part of it, was (in 1888) correctly rendered by the class-struggle ideology (see below p.) of the Manifesto—whereas it is equally clear that this was not the case for the large majority e.g. of the English and American workers and that, at best, only small minorities then followed the Marxist flag consciously

* The question of the achievements of the First International has been merged in mist owing to the joint efforts of its adherents and its enemies both of whom vied with one another for opposite reasons in exaggerating its influence. But it should be clear that it did not amount to a great deal, since the trade-union element that was represented lent but qualified support and since the rest of the membership consisted of persons whose own opinion about their importance was shared by nobody except a few police officers.

and intelligently. However, so imbued are many of us with the idea that the argument of the Communist Manifesto reflects either social reality or the modal workman's genuine attitude towards his class position in capitalist society that it seems worthwhile, before we proceed, to scrutinize this part of the Marxist saga.

The reader will presently be able to satisfy himself that I have no intention to minimize the intellectual performance embodied in the Communist Manifesto. But no amount of respect for it can alter the fact that its position in the history of socialist thought is closely wound up with the acceptance of Marxism, first, by small but efficient groups in France and Russia and, second and more important , by the great social democratic party of Germany (Erfurt Program, 1891). But this acceptance which raised the Manifesto to the place it occupies now was not a conversion to the one and only possible truth, not a victory of light over darkness, not the socialist day of Damascus, but a tactical move that was very possibly a tactical mistake—as the comparison of German and English developments suggests. Some doubters—not less stalwart socialists than the Marxists—arose practically at once and the revisionist controversy was in full swing before long. And if the Party was unable to make short work of these doubters but had to be content with a formal recantation that did not mean much, this was because the masses, especially the trade unions, responded to them and failed to take kindly to the class-struggle philosophy of the Manifesto. True, extensive pedagogical efforts in the party school eventually did convert an increasing number of them, but substantially that situation—the unavowed rift between the Party which was dominated by Marxist intellectuals

Article on the Communist Manifesto, handwritten and typed, 1 of 9

and the trade unions which were much more directly under the control of the workmen--persisted, and created difficulties throughout because the masses felt that the Marxist ideology was not their own but that it was imposed upon them by intellectuals who had adopted another intellectual's idea of what their ideology ought to be and who thereupon fought for it with all the energy which a group's instinct of self-preservation can supply.

Article on the Communist Manifesto, Marchewski

II

All that matters for us, within the limited purpose of this paper, is to be found in the first of the four sections of the Manifesto. Not that the other three are uninteresting: here and there, we are impressed by a sparkle or an arrestingly bitter phrase or a clever squib though on the whole not than we ? expect to find in documents of this kind. But they belong to the historian of political thought rather than to the historian of economic analysis. We may therefore deal summarily with them.

Let us glance at the last section first, the one that issues in the resounding call—"workingmen of all countries, unite!"—and, immediately before that, the treacherous phrase which sounds so wrong in the light of more recent developments, namely, that in a revolution "the proletarians have nothing to lose but their chains." For the rest, this section discusses the principle of temporary tactical alliances with non-socialist parties and in its two pages contains a number of statements that Marx and Engels felt to be absolute in 1872. We also notice, with a wry smile, the admonitory statement that "communists disdain to conceal their views."

A single remark will suffice for the third section on Socialist and Communist Literature that is devoted to the inevitable task of discrediting all the groups that sponsored competitive (and highly substitutable) currents of thought. Everything considered, the job is well done and our quarrel should not be with what Marx and Engels wrote but with those who take this sort of thing seriously. There is however a point about this series of vituperations that is of interest to the man primarily concerned with analysis. Each indictment—especially that

of the "reactionary" socialism of the feudal and official classes and that of the pseudo-socialism of the bourgeois class, not so much that of the utopians--is drawn up according to a definite schema. Marx and Engels realized that every group or "movement" needs some ideas with which to verbalize itself, some interest from which to derive support, and some organization through which to act. Within their general frame of thought (see below III) this conception took a particular form: the interest was defined as economic class interest; the organization as well as the ideas were purely derivative and determined by the circumstances of the class and the means that its position in the economic and social structure put within its reach. And they proceeded to analyze the various types of socialism and quasisocialism at which they aimed in terms of this method. They refrained of course from applying the principle involved to Communism of their own brand but, however distorted by the bias inseparable from their polemical purpose, it worked fairly successfully with "feudal" and bourgeois socialisms or reformisms: there is, e.g., a considerable amount of truth, even though not the whole truth, in their analysis of the manner in which sectors of the aristocracies and gentries of Europe were driven back upon pro-labor policies by the rise of the bourgeois power.*

* The spiteful subsection on German or"True" Socialism (subsumed in the category of Reacting Socialism) should not go unmentioned. It is disfigured by personal resentments that are natural in a man who once had been a would-be Privatdogent but it contains some things that are not only amusing but also have the kind of truth that is in every malevolent caricature. I could however not hope to earn the gratitude of my readers by going into this matter.

In the second section Marx and Engels attended to two very necessary tasks. The one was to protect the communism they meant to stand for against popular aspersions. Following a hallowed practice of all ages, they selected these

aspersions wisely and stated them at the lowest possible level--just as radicals do today. Aided by this device, they did a good job--a masterpiece, in fact, including the opponents strong points--replacing fact and reasoning by emphatic assertion--"the workingmen have no country"--whenever convenient. The necessity of the other task arose from the fact that no group can do without an "immediate program" unless it is prepared to put itself (politically) out of the running. It was all very well to proclaim the principles of organizing the proletariat so as to enable "it"--Lenin was the first regular socialist to admit clearly that the proletariat never could and would emancipate "itself," i.e., without being officered by intellectuals--to step into the position of a ruling class, to conquer political power, and to wrest--but, mind, "by degrees"--all capital from the bourgoisie, "to centralize all instruments of production in the hands of the state. . . and to increase the total of productive forces as rapidly as possible"(l.c. p. 30).* But followers, if there were to be any, were bound to

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* This is as near as Marx ever went in drawing the contours of the socialist economy. As everybody knows, his scientific work was entirely devoted to explaining the capitalist process with a view to proving that it would, by virtue of its logic, turn into socialism. He thereby created a difficulty for his followers which they never overcame--this was done for them by economists of bourgeois complexion, especially by Barone. By implication,however, that passage in the Communist Manifesto covers more ground than it seems to do at first sight as the reader will easily perceive. Observe in particular that Marx--who thereby proved how deeply rooted he was in 18th century nationalism--took it for granted that the "proletariat," freed both from bourgeois inhibitions and from the capitalist whip would have no more pressing business than to enslave society's "productive forces." This belief shows up frequently in his writings.

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ask: Yes--but what now? And Marx faced the question.

In presenting his answer he was very obviously aware of a difficulty: the decalogue of measures he felt able to draw up was sure to read flat and insipid after all the glowing rhetoric that went before. So he proffered

comfort to the faithful, first, by calling these measures "despotic inroads on the rights of property and on the conditions of bourgeois production," *

* Thus, conservative Republicans of our day have the authority of Marx himself for calling "a heavy progressive income tax" a despotic inroad on the rights of property"—respectfully submitted.

and, second, by pointing out—very truly—that these measures "though economically insufficient and untenable" tend to "outstrip themselves" and will necessitate further inroads upon the old social order.

After this, no further comment is needed on the decalogue (l.c. p.30) from the abolition of property in land and the heavily progressive income tax, through the governmental national bank and the "extension of factories. . . owned by the state," to the free education of all children in public school, except this. Section 8 reads: "Equal obligation of all to work. Establishment of industrial armies, especially for agriculture. But for this one Hitlerian item the rest of the recommendations could have been taken from J. S. Mill's Principles* or, more precisely, there is, with that exception and possibly another

? * I do mean of course that they were so taken. The Principles appeared in 1848, but after the Manifesto.

that might have to be made regarding the extension of state-owned factories, nothing in the decalogue that Mill could have objected to on principle though he might have raised objections on grounds of practical difficulty. Anything that would have been incompatible with the bourgeois economics of the time—so far as represented by J. S. Mill—was conspicuous by absence, e.g. any tampering with profits or with free trade.

Article on the Communist Manifesto, handwritten and typed, annotated copy of 1848

III

For the purpose of analyzing the scientific contents of the Manifesto*—

*By anticipation, I thus recognize that the argument of the first section of the Manifesto does come within the range of empirical science. Nevertheless, I shall admit—and even emphasize—that it also formulates an ideology: in fact, I have done so already in the preceding part of this paper. There is, however, no contradiction in this: an ideological conception may be developed or implemented by scientific tools of analysis and a scientific piece of work may contain any amount of ideology, i.e. of extrascientific preconceptions. I hope that this will become clear as we go along (I have tried to explain this point also in my Presidential Address at the American Economic Association's Annual Meeting of 1948, see American Econonomic Review, March, 1949). For the time being, it is sufficient to state that ideologies are not necessarily "wrong," that is, not necessarily incapable of scientific verification and that, even if they are, they do not necessarily destroy the scientific nature and value of the analysis with which they are amalgamated.

Section I—we shall introduce a distinction that is not to everyone's taste and in particular entirely non-Marxist,* but presents decisive expository advantages,

*It is an essential feature of the Marxist system that it treats the social process as an (analytically) indivisible whole, and uses only one conceptual schema in all its parts. Example: most of us use the concept, Social Class, for the purposes of sociology only; in the "pure" economics of today there are no classes in this sense but only classes in the sense of economic categories, i.e. of sets of individuals that have some economic characteristic in common. But with Marx the social class that is a living, feeling, acting sociological entity is also the class of his economic theory. One can fully recognize and even admire the Marxist conception—from the standpoint of which the economic classes of "pure" economy look like bloodless spectres whose relations to one another are stripped of their "social content," as Marxists say—and yet consider it an impediment to effective analysis.

the distinction between Economic Sociology and Economics. By Economic Sociology (the German Wirtschafts-soziologie)we denote the description and interpretation —or "interpretative description"—of economically relevant institutions, including habits and all forms of behavior in general, such as governments, property, private enterprise, customary or "rational" behavior; by Economics—or, if you prefer, "economics proper"—we denote the interpretative description of the economic mechanisms that play within any given state of those institutions, such as market mechanisms. Or, to use a felicitous if not completely synonymous turn of phrase of Professor G. Colm, Economic Sociology deals with the problem how people came to behave as they do at any time and place; and Economics with the problem how they do behave and what economic results they produce by behaving as they do. No question of principle is involved in this distinction. It is simply an expository device that, in itself, is incapable of being "right" or "wrong" and is to be judged merely from the standpoint of the categories "convenient" or "inconvenient."

1. The Economic Sociology of the Communist Manifesto. The first section of the document leads up to a diagnosis of the social situation of 1848—evidently supposed to be within measurable distance of the fall of bourgeois society—by means of a historical sketch that has been rightly called, by Professor S. Hook, a"miracle of compression" and contains, more or less definitely, at least four contributions to economic (and political)sociology, all of them warped by ideological bias but all of them of the first order of importance.

a) The Economic Interpretation of History.* So far as I can see, the

* I take this opportunity to call attention to the new edition of Professor M. M. Bober's,

Article on the Communist Manifesto, handwritten and typed, completed 8 pages

historical sketch referred to describes change in social structures and in their cultural complements in terms of economic change alone—both as regards the manner in which "feudal society" had disintegrated and as regards the manner in which "bourgeois society" was disintegrating. Such events as the colonization of oversea countries that widened markets and, later on, steam and machinery that revolutionized industrial production and passed sentence of economic death on the artisan's crafts, hence on himself qua artisan, are clearly visualized as steps in a purely economic process that is conceived of as going on autonomously, according to its own law, carrying its own motive power within itself. And all the rest of social life, the social, political, legal structure, all the beliefs, arts, habits, schemes of values are not less clearly conceived of as deriving from that one prime mover—they are but steam that rises from the galloping horse. These two propositions define Marx's Economic Interpretation of History.* Marx may not, when he wrote the Manifesto, have been so fully in

* For Marx and most of his followers the "materialistic" aspect of this theory was of course very important. It should be observed however that no materialism—in the philosophical sense—is implied in its acceptance. All that is needed is assent to the proposition that the economic structure and an individual's or group's location in it exerts a very strong influence on his or its thought and behavior. This is quite compatible e.g. with a belief in the freedom of will or any other religious or metaphysical conviction for it is possible to admit that, statistically and historically, people yield to that influence and to hold nevertheless that, on metaphysical and moral principle, they are not absolutely compelled to do so. To this extent, the term materialistic interpretation of history or historical materialism is a misnomer. Furthermore—as has been admitted by several staunch Marxists, e.g. by Plekhanov—the economic interpretation of history per se does not condemn ideas, e.g. moral ones, to insignificance or e.g. artistic creations to dependence upon the prevailing mode of production so completely as my own analogy with the steam that rises from the galloping horse might suggest: this analogy was intended to render Marx's own version of his theory, but now it is important to note that this theory retains meaning and, as a working hypothesis, usefulness if that version be modified. In fact, it is clear on the one hand that Marx's own account of the historical process implies the recognition of psychological links—forms of reaction—in its chain that are not reducible to "objective" conditions of production; and, on the other hand, that non-economic factors must enter the picture in order to explain why and how a given social situation, dominated by conditions of production, "produces" a phenomenon so completely incommensurable with them as is a given work of art.

Article on the Communist Manifesto, handwritten and typed, completed copy of 2 pages

possession of these two propositions as he was when he wrote the Preface of The Critique of Political Economy (1859, Engl. tr. 1911)—the almost desperate brevity of the Manifesto leaves room also for a somewhat different interpretation. But if he was then the birth of the economic interpretation of history dates from 1844.* Marx's originality and priority have often been called into question.

* But, unlike others, I do not find any traces of it in Marx's Holy Family of the same year.

But they are at least as good as Darwin's. Only St. Simon and perhaps L.v.Stein seem to me to have any right to figure as genuine forerunners; the cases for other candidates rest, I believe, largely on their sponsors' inadequate comprehension of what the economic interpretation of history really is—no more emphasis upon the historical importance of economic conditions or, still worse, interests** comes near it.

** It is relevant to note that even Engels, in his address at Marx's grave, defended historical materialism on the ground that, obviously, economic interests must loom large in any attempt at explaining the historical process. Unless we attribute this slip to an occasion that was not propitious to careful formulation this would mean that the loyal ally completely failed, in this point, to fathom Marx's thought. In some respects, the book he published under that title rather strengthens this suspicion.

Assuming, then, that Marx intended to present, by way of application, the economic interpretation in the Communist Manifesto we must, with a brevity that rivals that of the Manifesto itself, try to formulate an appraisal of the importance of this contribution to economic sociology. Of course, we shall do so in the light of the further information that Marx supplied in the Critique and in the first volume of Capital.

In the first place, it is a working hypothesis. Marx himself, as he tells us in the Preface to the Critique, considered it as "the leading thread in my studies." As such, it works sometimes extremely well, e.g. in the explanation of the political and cultural changes that came upon bourgeois society in the course of the 19th century, sometimes not at all, e.g. in the explanation of the emergence of feudal domains in western Europe in the 7th century—where the "relations of production" between the various classes of people were imposed by the political (military) organization of the conquering Teutonic tribes. We may indeed qualify the hypothesis—in various ways—e.g. by allowing for the effect of past conditions of production—or else define the concept of relations or conditions of production so widely as to include almost all the relations and conditions observable in human groups. But the reader will readily perceive that on this road we rapidly lose not only the glamor but also the explanatory value of the hypothesis. Still if we do not go too far on it some of both the glamor and the value may be salvaged.

In the second place, it must not be forgotten that Marx, deeply rooted as he was in 18th-century ideas and in the German philosophy that continued 18th-century traditions had an enemy to fight and an obstacle to overcome that barred the way toward an acceptable theory of history, the doctrine of the "general progress of the human mind" that made a purely intellectual process the causally important independent variable in social history—the doctrine that prospered so well from C to Comte and J. S. Mill. If the economic interpretation had done nothing else except to beat back—it did not accomplish more—this kind of thing by compensatory overemphasis upon "objective" economic conditions it would, because of this merit alone, have to stand high in the history of economic

as well as of general sociology. On this score, historiography, especially German historiography owes much to it.

In the third place, finally, the Marxist proposition that it is not man's conscious thought which determines their modes of existence but their modes of social existence which determines their conscious thought (Preface to the Critique)—which anticipates so much of later psychology—is readily recognized as a major contribution toward the theory of economic and political behavior and as a big step away from uncritical individualism even though we may not be prepared to accept it as it stands.

b) The Marxist Theory of Social Classes. The text of the Manifesto begins with the sentence: "The history of all society that has existed hitherto is the history of class struggles."* Neither for historians nor for sociologists

*To the edition of 1888, Engels added a qualifying footnote (in which he refers to his own Origin of the Family, Private Property, and the State) which limits the proposition to societies other and later than "primaeval village communities" which he seems to have regarded as classless and communistic.

or economists were social classes a discovery—for the economists the less so because most of them, and especially the English classics, had at that time not yet fully adopted the distinction between social classes and economic categories but were still in the habit of using the sociological entities, laborers, capitalists, and landlords, in their economic reasoning**—for Ricardo, the

**Throughout, Marx saw a decisive merit in this and was correspondingly severe on those who like J. B. Say had begun to divorce economic categories from the social classes of sociology. Needless to say, he knew why: the divorce might spell an advance in analysis but it tended to obliterate the all-important class antagonisms.

Attorney General was not yet a laborer like the street sweeper. Nor was it necessary to discover that every type of class structure, whether loyally

recognized or not, spells super- and subordination--every schoolboy knew this. Finally nobody can ever have failed to see that class structure is the source of many groupwise antagonisms--the most unhistorical economist must have heard of peasant wars and hoc genus omno. Nevertheless Marxists are right in claiming that the sentence quoted contains the principle of a theory of the social process that was novel and specifically Marxist in the same sense as was the economic interpretation.* This theory may be conveyed in three steps.

* That is to say, there were a number of forerunners of whom, once more, St. Simon was the most important; but we may still attribute to Marx--in the sense that may be again illustrated by the, in this respect, analogous case of Darwin's theory of natural selection--a theory which he stated and developed with insurpassable force. In view of the connection which will be presently indicated between the Marxist theory of social classes and his formulation of the economic interpretation of history it is important to observe that the two are not logically inseparable i.e. that they do not naturally imply one another. A little reflection will satisfy the reader that it is possible to hold each of them without holding the other.

First, Marx's classes are defined exclusively in economic terms: the social process of production determines the classwise relations of the participants and is the "real foundation " of the legal, political, or simply factual class positions attached to each. Thus, the logic of any given structure of production is ipso facto the logic of the social superstructure.* This is so obviously untrue

* In expounding Marx's doctrine on classes I continue to borrow from his later works particularly the Critique and the first volume of Capital. But I do not think that I thereby read anything into the Manifesto that is not there. I have not even the slight doubt that, as the reader will have observed, made me hesitate in the case of the economic interpretation of history. Even the significant term class culture occurs in the Manifesto: this part of Marx's ideology or analysis, then, was, so I believe, fully developed (never to be altered) by 1847.

that it seems more important than to show this to warn the reader against

jettisoning a ? a proposition that, though untenable, does contain an important element of truth: no class can keep a position above the proletariat—not at least anywhere outside of utopias—without some, even though possibly modest* economic complement for which, accordingly, it is in most cases ready to fight, and the increase or decrease of which is, also in most if not all cases, correlated with the increase or decrease of its social weight. The objection to Marx's theory is not that he saw and emphasized this element but that he related the class phenomenon causally to it: in many cases, the causal nexus is the other way round; in all the others the nexus between the structure of production and the class structure embodies at best an immediate cause through which analysis must cut in order to reach more fundamental ones.

But Marx weakened his economic theory of the class structure still further in order to fulfill his ideological desire to come out with the great battle array between bourgeoisie and proletariat. For pre-bourgeois society he was ready enough to recognize a complicated interplay of a multiplicity of classes that keeps more closely in touch with observed reality. He also recognized that these pre-bourgeois classes are hardy plants that take a long time in dying. As a tendency that was bound to prevail in time he held that society was more and more splitting up into those two "hostile camps." The difficulty with this is not that the persistence of the "old" middle class, the farmers or peasants and the artisans, might defer socialist possibilities to an indefinite future, or even that this "old" middle class might altogether fail to disappear. The difficulty is that the capitalist process creates a "new" middle class that

* "Modest" refers to the share of the individual member only.

fills continuously the whole range between the grande bourgeoisie of which Marx was thinking and half-starved laboring masses and, bordering on the very rich and the very poor, and sometimes hostile to both, constitutes a "class" of its own. Observe: such a pattern does not necessarily preclude advance toward socialism; but it might preclude advance toward socialism on Marxist lines and for Marxist reasons.

Second, it is characteristic of Marx's theory of classes that the class-wise relations determined by the structure of production are exclusively viewed as antagonistic. From first to last, Marx seems to see nothing but opposition of interests between them: essentially and inevitably, their relations to one another isstruggle (class war). And from first to last they are relations between oppressors and oppressed, exploiters and exploited. If these and similar terms meant nothing but value judgements there would be nothing more to be said--everybody, if he so pleases, is free to consider himself exploited by the (n-1) other inhabitants of the globe. But the analyst who means more than this, is not free to give in to what is clearly an ideological postulate.* The complex

* Of course, by class antagonism Marx meant (and so do I) only the "objectively" determined opposition of classes. He didnot mean (and neither do I) conscious hostility or will to hurt and fight although these things do enter into his class-consciousness which he was trying to teach the proletariat. He even went so far as to say that the immediate aim of the communists is "formation of the proletariat into a class" for the conquest of political power (l.c. p.22). This looks like a slip at first sight, and in a sense it was. But we may correct it into "to awake the proletariat to its class position."

of individual and group relations contains as many or more strands of cooperative than strands of antagonistic color and in addition others that change their color according to circumstances.* Still, the antagonisms exist--though they are

* "Objectively" speaking, see preceding footnotes. The psychological reflexes of the objective state of things are not without importance, but they are another matter.

Article on the Communist Manifesto, hand-written and typed, completed copy of CM

frequently sectional ("vertical") rather than classwise ("horizontal"). And there is some excuse for "compensatory overemphasis" on them--though Marx's attempt to substantiate them in his economic theory--i.e. by his exploitation theory of interest--was a complete failure.*

* I shall say at once that no such attempt was made in the Manifesto: several passages point toward, but do not amount to, a theory of this type.

Third, it was this conception of the nature of social classes and this conception of the nature of their relation to one another which Marx chose for pivots of his theory of history: it is they which, in his system, implement the economic interpretation of history. Now let us carefully distinguish two different and separable aspects of this.

In the first place, we have already observed that the economic interpretation of history--no matter whether or not we accept Marx's formulation of it--can also be implemented, i.e. be made to work as an instrument of explanation, in other ways: there is no need to graft a theory of classes upon it and to make such a theory of classes, whatever it be, the only link between the economic interpretation of history and everything else, especially the explanation of the economic process.** But, if this be done, it can be done also by means of other

** This statement is not intended to convey a criticism. Every Marxist can accept it because acceptance would still leave him free to hold that implementation of the economic interpretation by means of a theory of social classes is the "best" or even the "only true" manner of implementing it. I am only trying to emphasize once more that to do so means the introduction of a new idea not already contained (logically implied) in the economic interpretation.

conceptions of the nature of social classes and their relations to one another. And if in this case a quite different picture of society should result, the man who paints it would still have to acknowledge indebtedness to, or at least

the priority of, Marx's picture. In other words: the idea of making social classes and relations between them the pivots of the historical process, and of speaking of class culture and so on, *might* prove analytically valuable, even if we refuse to accept Marx's particular theory of social classes.

In the second place, however, Marx thought of *his* social classes and *his* idea of their relations to one another when he penned the first sentence of the Communist Manifesto. Everywhere in history he saw—and everything in the historical process he interpreted in terms of—the purely economic classes of his schema and their "struggles," veiled or open: the historical process was a resultant of opposing forces and these opposing forces themselves were essentially the forces of opposing classes rooted in the prevailing structure of production. Of course *this* theory is but a special case of the one at which we have glanced in the preceding paragraph—and infinitely more bold and definite. But once more: should we find reasons to reject it, the ones alluded to before or others, and even to vote it an ideological delusion of the uprooted *bourgeois* revolutionary, we shall not be compelled thereby to reject also the more general theory.

c) *The Marxist Theory of the State.* Policy is politics. There is no scientific sense in economists sitting down in the seat of judgement and in pronouncing upon the Common Good or Social Justice without specifying which of the many—and totally irreconcilable—meanings of these terms they have chosen to adopt. And to speak of a State and of Public Policy that, sailing with the clouds, are exempt from and above human struggles and group interests is, well, just bureaucratic ideology and just as reasonable as it would be to speak of business as an agent that satisfies the material needs of humanity without any regard to the businessman's interests. It is really surprising that economists

should have, almost to a man, been blind to these facts and that they should have failed to see the counterpart of the profit motive that shapes Public Policy as much as the businessman's profit motive shapes business behavior.*

*The political profit motive is not of course to be defined in terms of money but of political position and office. But it is not less real for being less measurable. The cases in which political behavior cannot be defined in terms of "political profit" strengthen the analogy instead of weakening it: for business behavior deviates from the course presented by the motive of business profit not less often.

The outstanding exceptions are some of the English classics and particularly A. Smith who argued, e.g., for laissez fair as much because of his clear perception of what politics and the politicians are as he did on purely economic grounds.** It was therefore a major analytic achievement that Marx saw this

** Analysis of the argument of Book IV of the Wealth of Nations makes this very clear.

problem and made the attempt to bring government, parties, and politics down from the clouds and into the sphere of realistic analysis.

Unfortunately, ideology--or the agitational purpose that must not be confused with honest ideological delusion--impaired this achievement. On the one hand he would have accepted my slogan--Policy is Politics--only for the pre-socialist world. When the proletariat will have destroyed capitalist property relations and capitalist class culture there will be--after a transitional stage--no classes, hence no class politics, "the free development of each" will be "the condition for the free development of all" (l.c. p. 31) the State will wither away and, as Lenin of all men was to aver, government of men will be reduced to government of things in the manner of a postoffice. No need to comment on this. On the other hand, for the world as it is or was, government or the executive in the modern representative State "is but a committee for managing

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the common affairs of the whole bourgeoisie" (l.c. p. 11)—and parties are identified, on principle at least, with (Marxist) classes. Blinkered narrowness that spoiled what might have been the foundation stone of a political science that is more than dreams and phrases! The question is not without interest what it precisely was that caused this miscarriage.

The first thing about the "economics proper" of the Communist Manifesto that must strike every reader and socialist readers still more than nonsocialist ones is this. After having blocked out the historical background of capitalist development in a few strong strokes that are correct*—starting from the widening

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of markets consequent upon the colonization of America, part India, and so on and the resulting breakings of medieval forms of production and ending up with the large-scale factory and steam and steel—Marx launched out on a panegyric upon bourgeois achievement that has no equal in economic literature. The bourgeoisie "has been the first to show what man's activity can bring about. It has accomplished wonders far surpassing Egyptian pyramids, Roman aqueducts, and Gothic cathedrals" and "by the rapid improvement of all instruments of production . . . draws all nations, even the most barbarian, into civilization. . . . It has created enormous cities" and "during its rule of scarcely one hundred years has created more massive and more colossal productive forces than have all preceding generations together." ", and so forth. No available comparable statement of what has any other time—certainly not A. Smith or J. S. Mill—can equal this. Observe in particular, the emphasis upon the positive role of the bourgeoisie that the majority of the more "scientific" socialists so philosophically condemn. And if the bourgeoisie—that is, some thirty odd of us really do this and work insert into the picture this pro-bourgeois contribution to the proletarian movement

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the contributions of a non-bourgeois bureaucracy for instance--and, on the other hand, commit the mistake (for such I believe it is) to list as independent factors science and technology whereas Marx's sociology enabled him to see that these as well as "progress" in such fields as education and hygiene were just as much the products of the bourgeois class culture--hence, ultimately, of the business class--as was the business performance itself. Never, I repeat, and in particular by no modern defender of the bourgeois civilization has anything like this been penned, never has a brief been composed on behalf of the business class from so profound and so wide a comprehension of what its achievement is and of what it means to humanity.

Whatever the function of these passages is in a document that purported to be the manifesto of a "party," there cannot be any doubt about their significance for economic analysis. And Marx did not lose the opportunity to add a number of touches that make this significance more precise.

First of all, the creative role of the business class is, by identity, a revolutionary role. This must not be taken as a mere reflex of Marx's philosophical position according to which any creative involved "revolution." The revolution in question is a "constant revolutionizing of production," creation that spells the obsolescence and consequent destruction of any industrial structure of production that exists at any moment. This is capitalism: capitalism is a process, stationary capitalism would be a contradiction in adjective. But this process does not simply consist in increase of capital--let alone increase of capital by saving--as the classics had it. It does not consist in adding mailcoaches to the existing stock of mailcoaches, but in their elimination by railroads. Increase of physical capital is an incident in this process but it is not its propeller.

Second, this incessant economic revolution tends to revolutionize the preceding social and political structure and class civilization. It breaks up the medieval environments that fettered but also protected the individual and the family. By destroying the feudal aristocracy, the peasants, and the artisans, it also destroys the moral world of feudal aristocrats, peasants, and artisans. It changes the mind of society. "It has drowned the most heavenly ecstasies of religious fervour, of chivalrous enthusiasm, of philistine sentimentalism in the icy water of egotistical calculation. It has resolved personal worth into exchange value. . .stripped of its halo every occupation hitherto honored and looked upon with reverent awe. . . has torn away from the family its sentimental veil" (l.c. p.11)—in short, it has created the godless utilitarian attitude to life. It has replaced "idyllic" traditionalism of the middle ages by haste and insecurity all round—for bourgeois and workman alike. Above all it has replaced the highly differentiated groups of the "oppressed" of old by what Marx finally believed was a homogeneous, nondescript, internationalist proletariat. All this is no longer "economics proper:" it is an essential link that connects Marxist economics with Marxist sociology and social psychology. And he who denies the force and grandeur of this vision is as hopelessly wrong as is he who takes it literally.

But, third, there are three purely economic features in that picture all of which were essential to Marx's vision of the capitalist process, all of which might be developed analytically in different directions, but none of which were formulated by Marx in such a way as to enable us to attribute to him definite "theories" of them.

To begin with, all economists know, at least by hindsight, that capitalism tends to evolve the giant concern—though some of us seem disposed to deny the

necessity of this feature of capitalist evolution. Marx saw it and saw its necessity (l.c. p.10) or thought he saw it but no professional economist will deny that much more than his hints at explanation would be necessary to establish it in a manner that would stand—or indicate that it could stand—scientific tests. Marshall's falling average-cost curves might be invoked along which firms, ever growing, rush on toward monopoly or oligopoly but there is no trace of this in the Communist Manifesto. Again, there are the "crises" that are adduced as an illustration of the proposition that "for many decades the history of industry and commerce is but the history of the revolt of modern productive forces against. . . the property relations that are the conditions for the existence of the bourgeoisie and its rule" and in which breaks out "the epidemic of overproduction." Except for the recognition of the phenomenon (also of its "periodicity") and its economic and political performance, this does not amount to much and is suggestive of Fourier's Crises plethoriques. If there be a theory implied in this passage (l.c. pp. 14-15) it is not the one that might be attributed to the full-fledged Marxist system.* Finally, there is the vision

*Marx never worked out any explicit theory of business cycles although his writings are full of fragments that his followers have tried to build into one. But it is safe to say that he outgrew both overproduction and underconsumption theories even though traces of both were retained throughout.

that the capitalist process not only creates the "proletariat" but also, by virtue of its inherent logic, steadily deteriorates its condition. It is this element which is supposed to account for capitalism's (imaginary) inability to do what every previous form of society had been able to do, vis. to feed its slaves or serfs—"and here it becomes evident, that the bourgeoisie is unfit any longer to be the ruling class," and that "its existence is no longer compatible with society (l.c. p. 21). This foreshadows that breakdown theory which

Marx was to develop in the first volume of capital and which, after many prevarications, was eventually abandoned by his followers. But in the Manifesto it lacks even so much substantiation as it was to receive later. All that is offered in support of the contention that real wages tend to decrease is that "the price of a commodity, and therefore also of labor is equal to its cost of production" and that "the cost of production of a workman is restricted, almost entirely, to the means of subsistence that he requires for his maintenance, and for the propagation of his race"—which sounds like highly Ricardianism (l.c. p. 16). Except for this passage which is clearly inadequate to establish the contention, the Manifesto displays even less training in technical economics than we might be disposed to attribute to Marx in 1847. So far as these purely economic items are concerned, there is not even much that is specifically Marxist, that is, much that anticipates Marx's technical economics of the 1860's. The word exploitation occurs, but there is little to point toward the particular exploitation theory he was to develop. "Capital holds pride of place but there is nothing of the elaborate capital theory of his later days. In the matter of value, there is that indication that Marx then followed, more or less, the Ricardian version of A. Smith's theory but no sign of what he himself was to make of it eventually.

All this, I think, answers the problem of the place of the Communist Manifesto in Marx's own development as an economist. This answer agrees both with the available evidence and with the opinion of Marxists. The known facts of his career as well as the story he told in the Preface to the Critique of Political Economy* make it practically certain that up to and including 1843 he had not

* The word Critique should not be taken in the sense it carries in common

parlance but in the sense it carried in the German philosophy of that or, rather, a somewhat earlier time--the analogy with Critique of Pure Reason will convey the point, especially if we remember that by Political Economy Marx did not mean the science or literature of Political Economy but the subject of it--the economic process itself.

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taken any serious interest in economics. The desultory reading, mainly of the works of French "utopian" socialists, he may have done before amounted to as much as such desultory reading means to the average educated person though any such person would believe himself to be getting along much faster than he does. In Paris, partly led on by Engels, he made more substantial progress but principally on the line of economic sociology as was natural for a man who came from philosophy. Even by 1847 he was hardly an economist at all: it was during the 1850's that he became one, and one of the most learned ones who ever lived, working away in the British Museum and the dingy apartment in Dean Street for what he was worth. But the social vision his work was to implement was quite set when he wrote the Communist Manifesto, though, again, more as regards economic sociology than as regards economics. Nothing essential was ever added to it or jettisoned from it. And the vision implied a program of research although it did not imply, to any great extent, technical economics--some of which in fact remained a non liquet to the end.

It seems to me that it is not more difficult to define the place of the Communist Manifesto in the development of our science. But acceptance of the way in which I am going to define it depends in turn upon the reader's willingness to accept something else. I have tried to explain that, in the history of political thought and of human creeds, the Communist Manifesto stands where it does by virtue of glory that is reflected upon it by later events: at the time it was published and irrespective of the adoption of the Marxist creed by the German party in 1891, which was to some extent fortuitous, itdid not amount to much.

Something of this kind is also true of its historical importance in our science. Itdid not make scientific history, and so far as its author did--even here the political alliance must not be entirely forgotten--he did so by virtue of his later work. If nevertheless we telescope part of his influence back into the pamphlet of 1848, we do so on the understanding that there may be point in speaking of the historical importance of a vision and a program when both meet with success in due course. By a fortunate coincidence, J. S. Mill's summarizing presentation of the economic sociology and of the economics of the period that appeared in the same year, may serve for background. Of course, we must discard all the differences that exist between a program and a finished treatise. Still more obviously we must discard Marx's prophetic wrath that was and is so irresistibly attractive to the sophomoric mind. What, then, could Mill, considered as a research worker only, have learned from the Manifesto?

No matter what Marxists may say, especially those of them, if any, who still have retained Hegelian propensities, he could not have learned much about aim and method. A characteristic, and a merit, of Marx's conception of his analytic task was indeed that it spelled the union of history and theory--that his history was to be theory and his theory history. But J. S. Mill did not lack this conception any more than Marx lacked the conception of what the proper place was for "deduction." They were both of them philosophers, philosophers who belonged to radically different schools and who would never have succeeded, even if they had wanted to, to find common ground epistemologically speaking. This however mattered little for their analytic practice and the absolute (Marx) or abstract (Mill) "laws" they turned out.

But this is true only so long as the term Methodology is restricted to <u>logical</u> properties of procedure. Beyond the limited range of methodology in this sense

there was a gulf between them: Mill's analytic structure centered upon what he called statics* and Marx's upon the "economic law of motion." It is true that

* He understood by statics pretty much what we ourselves understand by it. His method is perhaps best described as Comparative Statics.

Mill's treatise contains something on economic evolution and that when Marx's vision matured a stationary model, the model of Simple Reproduction, put in appearance. And it is not true that Mill was less aware than was Marx that capitalism was a passing, a historical phase of social history. He emphasized this again and again and the assertion to the contrary that Marxists seem never to get tired of repeating is the more unjustifiable because Mill too assumed that some sort of socialism, though of an associationist type, was the heir apparent. But Mill treated the problems of the process so cavalierly--he saw little more in economic evolution than a race between population and capital which the latter was destined to win--that Marxists would be right in protesting against comparison. Here,then,he might have learned a fundamental truth, if indeed he was capable of doing so. For in this point, there was not only a gulf but a difference in level that looks hopeless. As a matter of fact, Marx's sketch failed completely, even later, to inspire either socialists or non-socialists.

However, his economic interpretation of history and his doctrine of the classwar did inspire later historians and economists far beyond the circle of the orthodox Marxists. I wonder what J. S. Mill would have said about both. For him, economic institutions were just data, historically variable no doubt, but still something that is given to the analyst of economic phenomena, something

that comes within his range only by way of his task to analyze--and, of course, to judge!--their effects. There is a passage in Book II of the Principles that might be construed as a glimpse of deeper insight. But I rather think that an appropriately reformulated economic interpretation might have meant a new world to him. As regards Marxist classes and the Marxist classwar he would presumably have thought it unnecessary to go beyond his "sinister interests." Where he really scores, however, is pure economics. Perhaps there were a few things for him to learn in the matter of "big business" and monopoly of which he hardly saw the problem in all its breadth and depth. But as regards crises he might have been the teacher. And it needs no emphasis that he was completely right in "seeing no reason for regarding the future of the working class as otherwise than hopeful."

Still more than Mill, the modern economist will find the argument of the Communist Manifesto full of holes and of loose ends. Nor does he need any teaching to the effect that capitalism is a historical intermezzo and that this intermezzo is drawing to its close. But in two respects he can reap benefit from that document of which he clearly stands in need. He might do worse than ponder on Marx's panegyric on bourgeois achievement and on its implications for economic analysis. And nothing would do him more good than to learn the lesson that economic life is a unique process in historic time that unfolds its meanings only over the centuries--instead of turning round and round forever on the arid soil of short-run analysis that makes such poor pasture.

The Place of the Communist Manifesto in the History of Econ. Analysis

by

D. A. S.

The purpose of this paper is to estimate - approximately - the position of the Communist Manifesto, first, in the history of scientific economics (I) and, second, in the evolution of Marx's scientific work (II). This purpose is narrower than the purpose of a centenary appreciation of that document might be expected to be, and (improper) neglect of many things that, from the standpoint of either Marxology or of political thought, might be considered as more important than what I mainly wish to say. Part at least of my readers may now see some justification in my trying to do that limited job. And some of the aspects to be neglected will not be entirely excluded. They will ~~come in~~ be noticed in order to provide a frame for my arguments. (I and II)

Article on the Communist Manifesto, 1

I.

Friedrich Engels' Preface to S. Moore's English translation of the Manifesto, dated London, January 30th, 1888, tells us all we need to know for our purpose about the nature ~~of the publ~~ of the publication, the conditions under which it appeared and its fortunes. Later research, including the work of the Marx-Engels Institute, has added a number of details and corrected others none of which is of importance to our purpose.*) But Engels' Preface itself is important for us in several →

*) ~~The only~~ the merely note, from Engels' preface, that the Communist Manifesto was written, in German, in January 1847 and ~~published in~~ "sent to the printer" [a small firm in London] in February; that the first French translation ~~French~~ ~~edition~~ became available before June of the same year and the first English one (in G. J. Harney's Red Republican, London) in 1850. But the first American ~~edition~~ translation was published in the periodical of a brokerage firm — Lordhall and Claflin's Weekly; that a Russian translation (Bakunin's) appeared in 1870, another (Plekhanov's) in 1882. ~~Translations in~~ There were several translations into other languages before the end of the 1880's, i.e. before the German Social democratic Party placed itself on Marxist ground. The authentic German edition of 1872 is of particular interest because of ~~the~~ Marx's and Engels' joint preface to it. No further data of this type are necessary in what is emphatically not an essay in Marxology.

ENGLISH CRITICS OF THE LABOR GOVERNMENT'S PLANNING

by Joseph A. Schumpeter

Very naturally, the number of critical reactions to the policies of the English Labor Government is formidable by now. In fact, I have given up collecting them. Remembering, however, the large gains that scientific economics gleaned from discussions ~~in use~~ on controversies on practical discussions in the past, it may be of some interest to select a number of contributions to the present controversy in order to ask the question what the gains to economic analysis amount to in this instance. Before embarking upon an attempt to give an answer it seems desirable to explain the severely limited purpose of this paper more fully.

To begin with we are not going to discuss at all or at least not more than incidentally the literature that has been produced in support of the policies of the Labor Government. The writings of the critics make a well-rounded subject that invites separate consideration quite apart from the decisive one, namely the consideration of space. Moreover, there are evidently other points of interest about the criticisms than the one signled out by our question. We might ask, for instance, who the men are who react adversely and who try to define why they do so and how far. But barring the little that will be said on this in this introductory section no attempt will be made in writing what might conceivably be an interesting piece of economic sociology.

Next, I wish to disclaim any intention of proffering any criticism of, let alone advice about, English economic policy itself. I should consider this nothing short of an impertinence and it is only with a view to clarifying the contours of the discussion that I am going to make the following remarks.

We must bear in mind that the economic policy of England in the time of the Labor Government consists,as English policy of any kind and at any time has always done, of a set of measures that are to deal pragmatically with a given situation and that it is dangerous and may be downright misleading to do what economists always like to do, namely to speak of general principles that are supposed to be premises of everything that is being done. Among others, two important consequences follow from this. First, intellectuals may, according to their various allegiances,describe or refuse to describe the Labor Government's policies as planning or a socialist planning with or without the addition of the hallowed phrase "in a free society." This may mean a lot to them but it hardly means anything to the realistic observer. England never has had a policy that would readily concord with any speculative system. No more has she now. Second, it is impossible to deny the compelling nature of a great many elements in her present situation. We might philosophize indeed on whether another policy--meaning by policy nothing but the sum total of what has actually been done--might not have produced another situation that would be more satisfactory to ninety-nine Englishmen and Englishwomen out of a hundred. But in order to do so, we should have to review everything that has happened since August, 1914. Such an investigation would indeed by of great interest in itself and would in addition lead up to a question of fundamental if only analytic principle: the question whether and how far a prolonged war will under modern circumstances deflect the social process, definitely and for good from the course that it would have otherwise taken. But we are not concerned with this profound question except for a very minor point that comes within its precincts: things being what they are, replacement of the Labor Government by a Conservative one would certainly make much less difference than both Conservatives and Radicals, at

least on this side of the Atlantic, seem to believe.

That compelling situation is a mixture of two sets of circumstances which theoretically should be kept distinct but which it is practically impossible to keep distinct because they mutually condition each other. The England of the first decade of this century was slowly changing in mind and structure. I do not think that any intelligent observer then doubted that the development was in the Laborite direction, that labor would rise to official power and that, having so risen, it would not have run England forever on private enterprise lines though it might have done so at first. This development would be far advanced by now in any case and it would largely determine the attitude of government--any government--to the present problems of postwar transition and of England's adaptation to a completely changed world. But it is these problems and not any general principles of a Laborite or Socialist nature which are the immediate concern: it is success or failure in grappling with these which matters primarily to politicians, although the dominance of the labor interest and almost complete eclipse of any other severely restricts the choice between different courses by imposing some and putting others out of court.

After Waterloo, England settled down to her peacetime work in a manner which I have never ceased to admire. Of course, I am not unaware of the later criticisms both of the financial and the labor policy of that time, but I think these criticisms to be entirely unhistorical, even so far as they do not distort the facts and overlook, through ignorance or worse, such things as the Public Work Program in a famous budget of Castlereagh or the not insubstantial concessions that were then made to the sponsors of monetary management. We see a nation that the Napoleonic wars had left with tremendously increased possibilities. We see that these possibilities were energetically exploited and that a political

class of unparalled ability carried out a flexible policy that was ideally calculated to facilitate this task. An economist might be forgien for describing one aspect of this policy as sacrificing the mass welfare of the moment for the benefit of the future of these very masses. Also, he might be forgiven for thinking that from the standpoint of that future that policy amounted to an almost ideal handling of the Saving-Investment process. Finally, he should be forgiven even if he is not for suggesting that a comparison of that policy with the policies after 1918 and after 1945 yields results that are apt to verify the oldest of old economic theories, among others the Turgot Smith Theory of Saving.

Facts would not even contradict the atrocious heresy that modern fiscal policies plus what is called planning are in themselves quite sufficient to account for some of the difficulties in long-run results and to produce a state of things that looks indeed like circular stagnation. But any such policy as that was politically out of the question already in 1919 and of course still more in 1945. If practically all the leading economists of England and in particular the late Lord Keynes have so resolutely set their face against what I am tempted to call the facts and if instead they have concentrated on paralyzing with a view to eliminating the rate of interest on managing, consumption, investment and credit, this is only in part to be attributed to new convictions arrived at from a new (!) type of analysis: in part, it was due to their old conception of their task as advisers of their nation. They rarely worked on facts or theorems in that spirit that accounts for the success in the physical sciences that is to say in the spirit of the search for truth. As quickly as possible, they always proceeded to "application" and recommendation and we shall understand

that if these are indeed the only goals of this unfortunate pseudoscience, then the argument that something or other is politically impossible will be as good as the argument that it is false. Present discussions in both England and the United States provide a particularly sad instance of this: a large majority of economists simply argues party cases.

It should surprise no one that under such circumstances criteria of failure or success of a particular government are not only as they always would be very difficult to establish but completely submerged in value judgements and social and political allegiances. Everyone, of course, speaks of some things being desirable and other things being undesirable, of ethical ideals and that sort of thing, meaning by desirability or ethical ideality simply the interests of the group with which he has associated himself. And so it is as easy, and this I want very strongly to impress upon the reader, to represent the results produced by the labor regime as complete failure as it is to interpret them as a striking success. On the one hand, for instance, one might point very effectively to the ridiculous vexations to which the details of private life are subject, to what looks like sabotage of enterprise and economic progress, to artificial scarcity that is the gift of a party that professed to turn its back upon the economy of scarcity, to irreparable losses in England's economic and political positions, to the creation of a system that seems to unite the shortcomings of both capitalism and socialism. It should be added that such criticisms could be substantiated both from a straight socialist and a straight private enterprise standpoint. But on the other hand it can be urged with equal justice that no economic breakdown has followed upon this war such as followed both on the Napolennic and on the first World War; that throughout the working

Notes and preliminary MSS for "English Economists and the State-management Economy"

classes have been spared any economic sacrifice and that already in 1947 they were on the whole better fed and much better provided with the workman's typical luxuries than they were in 1939; that the policy of suppressed inflation has in a sense justified itself; than England's inability to live without foreign aid amounts simply to her ability to tax foreign nations; and that the policies practiced have not prevented the situation from improving and from steadily approaching a national and international condition of self-support. I am not interested in placing myself on either of these standpoints, but I feel that if I had to I could make out a good case for either.* To do so, is the business

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* of every Englishman and Englishwoman who ought to know what kind of England they want, and in particular whether they wish to think of those who will come after them or to be content with the philosophy of "in the long run we are all dead." All I wish to say for myself is that if I had to I could make, so I believe, a very acceptable case for either standpoint.

But there is one point on which I wish to comment before embarking upon my search for economic wisdom to be gleaned from these writings. As already mentioned preponderantly they are critical, that is to say they accept the first standpoint. But they do so in a manner that has in one respect surprised me.

They argue indeed the case for a free price system and mostly also for decentralized private enterprise that knows so much better how to make the best of every individual transaction whereas centralist bureaucracy is bound to commit large scale mistakes and so on, on familiar lines. But not only do they do so on a purely utilitarian level where it is a question of a right proportion between peas and beans, they also do so within the new institutional framework of our time accepting among other things , or at any rate protesting but feeble against, the tremendous transfer of wealth that has been brought about. Let us consider for a moment what this means. It means practical impossibility of providing savings with which to finance industrial expansion and complete impossibility of founding private fortunes and sustaining anything like the upper income brackets of the old income structure. But does not this mean renunciation of the capitalist scheme of values and of capitalist civilization--not to speak about incentive or motive and so on? Is there really nothing to be said for this schema? Must those who put a positive value upon inequality really wait for a victory of Bolshevism to provide inequality by means of the privileges that the ruling circles of a Bolshevist party will enjoy? And if indeed that schema and the romance of capitalist success are things of the past, is there really anything to fight for? With due respect to peas and beans, are they really worth bothering about when a cultural world has passes away, and when workmen houses and social services are the only things that are to be attended to anyhow?

The problem of these unemployed workers presents monetarists in a quite the reverse of the majority of economists in spite of the fact that the main practical bar-
rier to the providing a scheme by which to demonstrate a number of propoi-
ns of elementary economic logic. This scheme is in fact no longer a bone of
contention between non-socialists and the majority of socialist theorists, for
r since Marshall and Barone and in our own era since D. Taylor, Lange, Lerner,
others, the mechanism of pure competition has been inserted into the Ideo-
ic of the socialist community. Therefore, we shall not be surprised to find
t practically all the critics of the labor movement including Professor
ek, the "liberal socialists" institute the studies and accordingly attack the
logy of theoretic controls actually practised. Neither is the semi-official
ologists lacking upon the superiority of the management that is supposed to dis-
logists private producers or traders. The general argument about their spec-
ed knowledge and promptness of reaction is effectively supplemented by
ther's facts about restrictionism. However, under present conditions, all
this leads us to the dawn of further problems rather than to any simple solution.*

* The price system theology admirably shown is well criticised in an article
by Mr Hubert Henderson in the Economic Journal, December, 1940.

First, the English situation being one of suppressed inflation in a sense in
which ours is not, reestablishment of free markets is bound to produce a spell
of open inflation. If this inflation could be expected to go no farther than
present conditions warrant, this argument need not necessarily be very serious.
But it would certainly do more than that. Any considerable rise of absolute,
and readjustment of relative prices would upset the insecure truce that exists
in the labor market and create conditions in which inflation would intensify
and feed upon it[illegible]tinitely. Labor would fight the reduction in real
wages, the [illegible] remedy[illegible] for the situation, and insist on higher

money wages which in turn would further increase the price level and so on unless a radical monetary and fiscal policy were embarked upon in spite of the unemployment it would entail. In other words, reestablishment of free markets might mean a political and social showdown and, for a Labor Government, an impossible situation. It is true that our authors, in partial recongition of this, recommend only gradual repeal of direct controls and that in some cases their arguments really tell not so much against direct controls per se but only against particularly irrational ones. It is perfectly true that a number of administrative practices are strikingly suggestive of the regulations in force on the continent of Europe before the French Revolution or in Prussia before the Stein-Hardenberg's reforms in the first decade of the 19th century. To the outsider the fact seems particularly objectionable that in many cases three or four different permits, from different authorities, are required in order to attain a single economic end. Few people will deny that there is room for rationalization but this is a different matter. What I mean is that there is a more fundamental difficulty and that this difficulty seems to be taken to lightly. For instance, Harrod's energetic argument about the wastes of rationing and price control and his well-advised suggestions, e. g. for mitigating the effects of rise in rent, can hardly be said to matter. To avoid misunderstandings, I beg to state explicitly that the argument implied hasno application whatever to the entirely different problems of the United States. I can hardly conceive a situation in which the same policy in these matters would suit both countries.

I take this opportunity in order to express my surprise at the inadequacy of the theoretical backgrounds on which the discussion on onflation is carried on both in England and in this country. Most people will agree of course that the old quantity theory does not provide an acceptable basis. In fact, I confess

to a feeling that this opinion is, if anything, too widely and too energetically held, for a properly reformulated quantity theory is neither false nor useless under conditions such as the present ones. But I further maintain that what I conceive to be the modern theory of inflation is not less inadequate than is the old one. To choose for single criterion of policy that is repeated again and again whether a given move will immediately increase or decrease the inflationary gap is to misconceive the problem. This problem is, in the United States, so to adjust the economic process as to make it cease to produce further inflation in the long run. This involves attention to the saving and investment process and an attitude towards profits, taxation and wages that is best characterized by saying that it is the exact opposite from the one taken by the Federal Administration. In England, entirely different circumstances suggest a different attitude. But even there, Mr. Harrod's thesis that the root of the difficulty is excessive investment is at least misleading. Investment that will in the long run more than repay the expenditure involved or in other words investment of the kind that will rejuvenate the industrial apparatus and both extend it and keep it in shape in a time of rapid obsolescence seems to me to be much more likely than restriction about investment to remove the inflationary danger and to safeguard England economic future. It stands to reason that this in turn involves a fairly radical reconstruction of the present system of taxation. English literature is full of symptoms that this is in fact being increasingly realized. Even Meade the liberal socialist seems prepared to take more account of "incentive" than we were accustomed to find of late. But this is not enough. It should be really stated openly that English taxation such as it is would in itself suffice to produce secular stagnation and that no great increase in productivity can be expected from mere removal of direct controls so long as it remains as it is.

Notes and preliminary MSS for "English Economists and the State-managed Economy"

political preferences. Others on whom these books impinge in a mood of socio-logical thoughtfulness will notice the social philosophy at the back of every one of them, that is to say, the ideological allegiances or if you prefer the ultimate principles which they indicate. Such a reader will make a discovery that may come to him as a surprise. Excepting Professor Jewkes, who, from the first page of his introduction leaves no doubt that he is going to speak with moral pathos or in any case that he is going to voice the free-enterprise ethos, there is very little of either pathos or ethos in any of the books mentioned. Their authors write as if they were completely unaware of the fact that their economics bears upon something immensely more important than whether private producers or governments are more likely to decide satisfactorily upon the proportions in which productive resources are to be allocated to the production of peas or beans; that economic policy affects and is affected by the fate of civilizations, a social structure, a scheme of values, a mode of life; they treat economic problems as it were piecemeal, just as if they were of the same order with the problems of more or less efficient controls on a machine. Perhaps this is as it should be. Perhaps economists should never argue in any different spirit. But our sociology-minded reader will nevertheless ponder the fact that no socialist would write in this spirit; and that it is creeds and not logic which determines policies. He will indeed know of other books and articles in which the capitalist ethos is alive,* but very few of these are on the professional level. He will have to conclude that on this level the spirit is virtually dead or dying and to note this fact as one of the most significant straws in the wind. Economists who are Englishmen by birth and race do display more sympathetic understanding

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* An example is Government to Death, by Sir Ernest Benn, 19

Notes and preliminary MSS for "Right Economics and the State: Management Economy"

of the private enterprise system than do others. But the difference is not very great.

Notes and preliminary MSS for "English Economists and the State-managed Economy"

Notes Transcribed by Toni Slotkes

Notes found on desk, day of S.'s death, unfinished MS of "The March into Socialism"

Address A E A 30.XII 49

(Correlation between sympathy and prognosis)

I. Please do not misunderstand me: I do not advocate Socialism, nor measures to avert it. Socialism does not terrify nor attract me. I want nothing more than to diagnose our social situation, or rather a particular aspect of it.:

Taking for granted a long-run tendency toward socialism, I want to analyze the bearing upon it of the existing state of inflationary pressure.

Before I come to my subject, I want to present a few definitions and then briefly recall what I have said elsewhere about the long-run tendency.

(a) by (centralist) socialism I mean an organization of society in which the means of production and the decisions on what to produce and on who is to get which constitutes one of the tasks of public administration (call this perfect planning).

(b) by guild socialism I mean an organization of society in which the means of production, in every industry, are controlled by, and used in the interest of the workmen employed in it. I shall not treat this case beyond stating that the emergence of such a society is a possibility that should not be neglected (ability to pay; management).

(c) by the cooperative organization of society I mean an organization in which economic affairs are managed by vocational bodies, as adumbrated in the Encyclical Quadragesimo Anno. I shall not deal with this form of organization e either, beyond stating

1. that it may be the most important alternative to the omnipotent State within the pale of the Catholic Church;

2. but seems to be impractical without it.

Centralist Socialism, our topic, I cannot visualize except as bureaucratic socialism that would have to be "dicatorial" as regards the individual citizen. "Liberal" socialism seems to me to be not worth discussing except from a purely theoretical standpoint. But dicatorial socialism may be democratic in the sense

that government emerges from the competitive struggle for votes; or autocratic, like in Rudsia, in the sense that one man or group holds the monopoly of politicâ power.

I do not distinguish between socialism and communism, the latter having acquired a special connotation only bewause of the Russian element.

II. The long-run tendency toward socialism which I do not propose to discuss means simply the migration of economic affairs from the private to the public xp sphere; and the evolution of a new schema of values and a new style of life - a new civilization - that is produced by, and in turn reinforces, that migration (interdependence).

It can be shown, I believe, that the capitalist system itself, by virtue of its very economic performance, produces such a tendency and moulds our minds for an acceptance of a bureaucratic socialism in the sense defined.

This would be a slow process though its beginnings go far back into, and beyond, the epoch of 19th century liberalism. But the best way of satisfying ourselves of the existence of the tendency tuward bureaucratic socialism and the extent to which the free-enterprise engine is paralyzed already is to observe how far decay had gone by 1939 (equality, security, full employment) Labor market, money market; distrust in price mechanism; hostility to profit motive? item ~~(in interaction~~ Praeventiv-Irrtuemer wider current) and)to private thrift; taxation which began to look absurd - running after... defeating its own purpose; and that the short-run view began to prevail; and, very naturally, the world was swept by crisis hysteria - that turned oldfashioned bourgeois into étatists.

F a guess; "it is interesting that we commit preventive errors against the current"

(Withering away of the State: police and enforced obedience bigger than ever)

It is ttrue that in this country people fought shy of the word that did not tally well with time honored phrases.

It is also true that "subsidized freedom" readily granted to farmers and small m men of all types - these would-be exceptions.

It is finally true that - unforeseen by Marx but foreseen by Wicksell - even then a tendency was observable to eleminate an increasing sector of goods and services

Notes found on desk, day of S.'s death, unfinished MS of "The March into Socialism"

from the range of wants within which individuals were expected tp provide for themselves; and also that this is perfectly natural: education, hygiene and medical care, housing (plus heat and light) was, in Europe though more slowly here, increasingly considered to belong to the public sphere;

that compulsory consumption (is old) began to be added to gratis consumption, and this on an equalitarian basis though a New Inequality began to emerge (Russia);

That the destruction of the business man's autonomy was paralelled by an increasing destruction of the Consumer's Sovereignty (Interesting! the infinite variety of government)

We can call this Laborism (though farmers should be added): a free-enterprise system run within the empty forms of private enterprise and property, but for the benefit of labor, in which other interests only count so far as a case can be made out for believing that a policy favoring them will ventually redound to the advantage of labor.

(But nonsense to say that the State 'borrows'; sense of managed money

(Euthanisa of "rentier")

Also this Marx did not foresee;

But is it not an argument current in the U.S. that efficiency will overcome all that, and that it is better even for workers than the most excellent Marxism? There is something true in this - it could probably be had with an integration index of 300 at present prices, to have the distribution of 1929 and at the same time to fulfil all wishes! It is only a pity that it is not this which is desired.

III. But this process may be retarded or accelerated. Major wars - "total" wars in particular - accelerate it; see Europe after 1919, the special reason beign that the organs of the public sphere gain a position which they are slow to release, "using" everybody's fear of "return to normalcy", especially the clmor of the favored groups - many good arguments...Political weights are redistributed - even victorious wars now fail to strengthen the framework

Notes found on desk, day of S.'s death, unfinished MS of "The March into Socialism"

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(European States have no choice)

It is a particular aspect of this situation which I wish to analyze briefly: the situation of permanent inflationary pressure.

a) Public expenditure for

1. armament - G I bill (Have we inflation or deflation?)
2. foreign payments (Balanced budget neither/~~needed~~ necessary nor sufficient; neither monetary policy)
3. extension of the social services of the welfare state without tapping resources of the benefitted
4. Waste (Hoover) and subsidies

b) Pressure through money wage rate at high employment (reasonable to .!)

(4)

c) a full employment or stabilization policy which however makes redjustment impossible: there is common consent to ~~negotiate~~ inhibit every revision; the outcry at the slightest settling down backed by memories of 1921 or even 1929 to 1932

d) cheap money policy; consumers credit extension

e) vexations through anti-trust decisions

(Paradox of investment in England and, eventually, with us)

(Reductions would be of no use if economies are only to be used to pay taxes)

IV. Thus, partly purposefully, partly as consequence of the situation, the price level can only rise with all radicalizing consequences - this alone is an acceleration of the tendency.

~~But besides the remedies~~ But also show the remedies!

(Insert ~~a)~~ inflationary aspect also of a balanced budget "Taxing away savings")

~~b)~~ inflationary taxation (is inflation to favor profits)

~~c)~~ credit restrictions through interest rate or rationing would not be without influence on the output (gold)

c) direct ~~restrictions~~ ~~price fixing~~ cartels: price fixing, rationing, priorities

"planning and cartels "; but also subsidies will be still needed, and that is conquest by bureaucracy of private enterprise (perhaps also by way of credit when self-financing is impossible); frictions; deadlock; attributed to private enterprise

I do not say that any group follows this line on conscious purpose; this I do not know, and besides, such purposes are never wholly/~~entirely~~ conscious.

I do ~~not~~ say that a situation may emerge in which most people will consider complete

planning as the smallest of possible evils.

They will certainly not call it socialism or communism, and they will presumable make some exception for farmers, retailers and small producers.

But the free enterprise system is, as we said, a way of life and what is left of that, mere ceremonial, may not be worth bothering about.

Whether the American genius for mass production on whose past performance all optimism for that way of life rests, is up to this test, I dare not affirm, nor do I dare affirm that the policies respsonisble for that situation might be reversed.

Marx was wrong in his diagnosis of the manner in which capitalist society would break down, he was not wrong in the prediction that it would break down eventually.

Stagnationists are wrong in their diagnosis of the reasons why the capitalist process should stagnate.

They may still turn out to be right in their prognosis that it would stagnate - with sufficient help from the public sector.

The March into Socialism

by

Joseph A Schumpeter

I.

In order to minimize the danger of misunderstandings that is ever present in discussions on topics such as the one of this session I want first of all to settle a few preliminary points before taking up my subject which is the relevance, for the economic future of this country, of the ~~prospects~~ present state of inflationary pressure.

(a) For the purposes of this paper, ~~I~~ define ~~socialism~~ (centralist) socialism as that organization of society, in which the means of production are controlled and the decisions on how and what to produce and on who is to get what constitute ~~policy~~ are being made, by ~~the state~~ public authority instead of by privately owned and privately managed firms. All that we mean by March into Socialism is therefore the migration ~~of~~ of people's economic affairs from the private into the public sphere. Observe that, though both socialists and antisocialists ~~will associate such an organization with a number of other traits — that they like or dislike — as ourselves are not going to say anything about the kind of organization~~ have of course ideas of their own on the subject, it is hardly possible to visualize a ~~pure~~ socialist society ~~except~~ in this sense without a huge bureaucratic apparatus ~~except as managed by a huge bureaucratic apparatus~~ ~~If the apparent paradox that "classic" socialist institutions nevertheless describes which may or may not be controlled by

Main Paper

1b.

1. Joseph Schumpeter delivered his address, "The March into Socialism," before the American Economic Association in New York on December 30, 1949, from notes and not from a prepared manuscript. He was writing up these notes for the Proceedings and had all but finished his paper the evening before his death. He expected to complete it the next day (January 8, 1950) before leaving for Chicago to deliver the Walgreen Foundation Lectures. This paper is a first draft but carefully written in his own hand as were all his writings; there was no opportunity for him to make minor corrections or to write the concluding paragraphs. The corrections which consist largely in supplying punctuation or an occasional missing word have been kept to a minimum. The brief concluding paragraphs have been supplied by his wife from notes and memory.

Main Paper

note on page 1 b.

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THE MARCH INTO SOCIALISM

By Joseph A. Schumpeter
Harvard University

I

In order to minimize the danger of misunderstandings that is ever present in discussions on topics such as the one of this session I want first of all to settle a few preliminary points before taking up my subject, which is the relevance, for the economic future of this country, of the present state of inflationary pressure.

(a) For the purposes of this paper, I define (centralist) socialism as that organization of society, in which the means of production are controlled, and the decisions on how and what to produce and on who is to get what are ~~being~~ made, by public authority instead of by privately-owned and privately-managed firms. All that we mean by the "March into Socialism" is therefore the migration of people's economic affairs from the private into the public sphere. Observe that, though both socialists and antisocialists have of course ideas of their own on the subject, it is hardly possible to visualize a socialist society in this sense without a huge bureaucratic apparatus that manages the productive and distributive process and in turn may or may not be controlled by organs of political democracy such as we have today--a parliament or congress and a set of political officers who depend for their position upon the results of a competitive struggle for votes. Therefore we may equate the march into socialism to a conquest of private industry and trade by the State. The apparent paradox that this very same process is described by classic socialist doctrine as the "withering away of the State" is easily resolved if we take account of the Marxist theory of government. Observe

further that socialism does not exclude decentralized decision-making in the administrative sense--just as the central management of an army does not deny all initiative to commanders of subgroups. And observe finally that socialism in our sense does not necessarily--that is, by logical necessity--exclude the use of competitive mechanisms as we see, e.g., from the Lange-Lerner model. Freedom of consumers' choice and of choice of occupation may ~~be~~ but need not necessarily be restricted in socialist societies.

(b) I do not advocate socialism. Not have I any intention of discussing its desirability or undesirability, whatever this may mean. More important is it, however, to make it quite clear that I do not "prophesy" or predict it. Any prediction is extrascientific prophecy ~~that~~ attempts to do more than to diagnose observable tendencies and to state what results would be, if these tendencies should work themselves out according to their logic. In itself, this does not amount to prognosis or prediction because factors external to the chosen range of observation may intervene to prevent that consummation; because, with phenomena so far removed as social phenomena are from the comfortable situation that astronomers have the good fortune of facing, observable tendencies, even if allowed to work themselves out, may be compatible with more than one outcome; and because existing tendencies, battling with resistances, may fail to work themselves out completely and may eventually "stick" at some halfway house. Let us illustrate this point by point.

First, no competent--and, of course, sufficiently detached--observer of Russia in the Stolypin era could have diagnosed the presence of any tendency towards anything at all like the Lenin

system or in fact anything but rapid economic evolution and a ~~bigger~~ lagged adaptation of institutions to the results of that evolution. It was a war and the consequent military and administrative breakdown which produced the Bolshevist regime and no amount of unscientific determinism avails against this fact. Second, for the sake of brevity, I speak of centralist socialism only because it holds ~~honor of~~ a place of honor in the discussion. But other possibilities should not be neglected. Familiar facts of our own trade-union practice suggest that a development towards some form of guild socialism is not entirely off the cards. And other familiar facts suggest, that observable tendencies or some of them may be compatible with forms of social reorganization that are not socialist at all, at least not in the sense which has been adopted for this paper. For instance, a reorganization of society on the lines of the encyclical Quadragesimo anno, though presumably possible only in Catholic societies or in societies where the position of the Catholic is sufficiently strong, no doubt provides an alternative to socialism that would avoid the "omnipotent State."

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Third, most observalbe tendencies of any kind stop short of complete achievement. Thus, a socialist regime in this country would have to be bold indeed if it ever thought of touching the subsidized independence of the farmer. Even the position of the "small business man" ~~position~~ might prove too strong for bureaucracy to conquer and a large fringe may therefore be indefinitely covered by compromise arrangements. ¶ Still more important is something else, however. As economic cares migrate from the private to the public sphere, many urges that favor this migration become satisfied, wholly or partly, so that the tendency may lose momentum. Some economists will add that any gradual movement towards a centrally planned economy offers opportunity for

unfavorable ~~experiences to be made and to~~ developments to be experienced which may act as brakes. I have no time to explain the reasons why I do not rate either possibility very highly and why, in particular, results that are felt to be unfavorable by sufficiently important groups are more likely to exert a propelling than they are to exert a restraining influence; that is, that the remedy for unsuccessful socialization ~~that~~ which will suggest itself will be not less but more socialization. But for our purpose it is essential to notice that most of the arguments that are framed in order to arrive at a result favorable to the survival of the private-enterprise economy do not really deny the existence of a tendency towards socialism in our sense, but only deny that it will work itself out completely. Since nobody can ~~deny~~ dispute this possibility there is danger that the controversy resolve itself into a ~~mere~~ battle of words, especially in the United States where mere words count for so much, where the term socialism is not popular except with some relatively small minority groups, and where many people who like the thing at the same time dislike the word and prefer to substitute another, e.g., liberalism.[2] Hence a brief attempt at classification seems ~~hence~~ to be indicated.

(c) The reasons for believing that the capitalist order tends to destroy itself and that centralist socialism is--with the qualifications mentioned above--a likely heir apparent I have explained elsewhere. Briefly and superficially, they may be summed up under four heads. First the very success of the business class in developing the productive powers of this country and the very fact that this success has created a new standard of life for all classes has paradoxically undermined the social and political position of the same

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[2] ~~[illegible]~~ For obvious reasons, this is still more the case with the term Communism which, barring the Russian angle, should be used synonymously.

business class whose economic function though not obsolete, tends to become obsolescent and amenable to bureaucratization. Second, capitalist activity, being essentially "rational", tends to spread rational habits of mind and to destroy those loyalties and those habits of super- and subordination that are nevertheless essential for the efficient working of the institutionalized leadership of the producing plant: No social system can work ~~what~~ which is exclusively based upon a network of free contracts between (legally) equal contracting parties and in which everyone is supposed to be guided by nothing except his own (short-run) utilitarian ends. Third, the concentration of the business class on the tasks of the factory and the office was instrumental in creating a political system and an intellectual class the structure and interests of which developed an attitude of independence from, and eventually of hostility to, the interests of large-scale business. ~~which~~ The latter is increasingly becoming incapable of defending itself against raids that are, in the short run, highly profitable to other classes. Fourth, in consequence of all this, the scheme of values of capitalist society, though causally related to its economic success, ~~are~~ is losing their hold not only upon the public mind but also upon the "capitalist" stratum itself. Little time, though more than I have, would be needed to show how modern drives for security, equality, and regulation (economic engineering) may be explained on these lines.

The best method of satisfying ourselves how far this process of disintegration of capitalist society has gone is to observe the extent ~~of~~ to which its implications are being taken for granted both by the business class itself and by the large number of economists who feel themselves to be opposed to (hundred-per-cent) socialism and are in the habit of

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denying the existence of any tendency toward it. To speak of the latter only, they accept not only unquestioningly but also approvingly: (1) the various stabilization policies that are to prevent recessions or at least depressions; that is, a large amount of public management of business situations even if not ~~a~~ the principle of full employment; (2) the "desirability of greater equality of incomes", rarely defining how far short of absolute equality they are prepared to go, and in connection with this the principle of redistributive taxation; (3) a rich assortment of regulative measures, frequently rationalized by anti-trust slogans, as regards prices; (4) public control though within a wide range of variation over the labor and the money market; (5) indefinite extension of the sphere of wants that are, now or eventually, to be satisfied by public enterprise, either gratis or on some post-office principle; and (6) of course all types of security legislation. I believe that there is a mountain in Switzerland on which congresses of economists have been held ~~that~~ which have expressed disapproval of all or most of these things. But these anathemata have not even provoked attack.

It would spell complete misunderstanding of my argument if you thought that I "disapprove" or wish to criticize any of these policies. Nor am I one of those who label all or some of them "socialist." Some have been espoused, ~~already~~ even in the ~~18th~~ eighteenth century, by conservative or even autocratic rulers; others have been on the programs of conservative parties and have been carried by them long before New Deal days. All I wish to emphasize is the fact that we have traveled far indeed from the principles of laissez-faire capitalism and the further fact that it is possible so to develop and regulate capitalist institutions as to condition the working of private enterprise in a manner that differs but little from genuinely socialist planning. The economists I have in

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mind no doubt emphasize the differences they think likely to persist. They are not all agreed as to the precise location of their ~~no doubt~~ movable half-way house. But they all realize what Marx failed to realize: on the one hand, the vast productive possibilities of the capitalist engine that promise indefinitely higher mass standards of life, supplemented by gratis services without complete "expropriation of the expropriators"; on the other hand, the extent to which capitalist interests can in fact be expropriated without bringing the economic enging to a standstill and the extent to which this engine may be made to run in the labor interest. Having discovered this possibility of a laborist capitalism they go on to conclude that this capitalism may survive indefinitely, at least under certain favorable conditions. ~~That~~ This may be so but it does not amount to a denial of my thesis. Capitalism does not merely mean that the housewife may influence production by her choice between peas and beans; nor that the youngsters may choose whether he wants to work in a factory or on a farm; nor that plant managers have some voice in deciding what and how to produce. It means a scheme of values, an attitude toward life, a civilization--the civilization of inequality and of the family fortune. This civilization is rapidly passing away, however. Let us rejoice or else lament the fact as much as everyone of us likes; but do not let us shut our eyes to it.

One genuine problem remains. The diagnoses that support implications ~~that~~ which are favorable to the survival of laborism all lean heavily on extrapolations of the present spectacular development of society's productive powers. But there is an element of question-begging in this. Past achievement was the achievement of a more or less unfettered capitalism. It cannot be assumed without ~~any~~ further consideration that laborism will continue to perform like this. We need not accept the stagnationist

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thesis as it stands in order to be disturbed by the possibility that this thesis may come true after all if the private-enterprise system is permanently burdened and "regulated" beyond its powers of endurance. In this case, an outright socialist solution may impose itself even on ~~its~~ the enemies of socialism as the lesser evil.

II

The transformation of social orders into one another is an incessant process but, in itself, a very slow one. To an observer who studies a moderate span of "quiet" time, it may well seem as if the social framework he beholds did not change at all. Moreover, the process often suffers setbacks which, considered by themselves, may suggest to him the presence of an opposite tendency. But at times we also observe accelerations and one of the most obvious causes of these are major wars. In the past, successful wars may have added to the prestige of the ruling stratum, and to the strength of the institutional framework with which this stratum was associated. This is no longer so under modern conditions. The first World War of our own epoch affected the social situation in the United States but little because the war effort was neither enough exhausting nor enough prolonged to leave a permanent mark. But in Europe it was different. In the vanquished countries where the social framework caught fire, the latent tendency toward socialist reconstruction proved its existence by emerging to the surface and, for a brief period, carrying everything before it. Still more significant is the fact that something similar also happened, though of course on a much reduced scale, in the victorious countries. In France the bourgeois republic ceased to function as it had ~~#~~ functioned before 1914. In England, a labor party that was ~~indeed~~ not yet socialist but was influenced by a socialist wing, rose not indeed to powe

but at least to office. And in both countries, the attitude of the political sector to the private-enterprise system underwent quietly a fundamental change.

Given a preexisting tendency toward the socialist goal, this is easy to understand. Although voices that called for a continuation of the policies established during the years of the war economy did not elicit much response and although, for a time, public resentment of war regulations blocked further advance on the same lines, no return to prewar policies proved possible even where it was attempted. This has been strikingly verified by England's gold policy and its ultimate failure. In a world that was no longer the world of free enterprise, the gold standard--the naughty child that keeps on telling unpleasant truths--refused to work.

The world crisis and the second world war were additional "accelerators" and, this time, they asserted themselves also in the United States. They created situations that were felt, rightly or wrongly, to be beyond the remedies that would have recommended themselves to the men of the free-enterprise age. The business class itself, afraid of the "adjustments" that application of those remedies would have required, accepted--though of course grumbling all the time--gadgets of regulation ~~of this~~ ~~regulation~~ that might prevent the recurrence of the experiences of 1929-1933 and later on others that might prevent a postwar crisis such as that of 1921. It has learned much and unlearned still more during the last quarter of a century. Also, it has accepted new fiscal burdens a mere fraction of which it would have felt to be unbearable fifty years ago--as would, by the way, all the leading economists of that time. And it does not matter whether ~~it~~

~~////////////

the business class accepts this new situation or not. The power ~~or~~ of labor is almost strong enough in itself--and amply so in alliance with the other groups that have in fact, if not in words, renounced allegiance to the scheme of values of the private-profit economy--to prevent any reversal ~~that~~ which goes beyond an occasional scaling off of rough edges.

Let me repeat: I do not hold for a moment that any mere "events", even events of the importance of "total wars", or the political situations created thereby or any attitudes or feelings entertained by individuals or groups on the subject of these situations, dominate the long-run contours of social history. These are a matter of much deeper ~~factors~~ forces. But I do hold that such events and the situations created thereby may remove obstacles from the path of the more fundamental tendencies, obstacles that would otherwise slow up the pace of social evolution. Observe that this does not necessarily constitute a reason for a serious socialist to welcome such events. Evolution towards socialism would be slower in their absence but also steadier. Setbacks and the emergence of an unmanageable situation would be less likely. Coordination of developments in the various sectors of national life would be more perfect. For, just as the existence of an efficient opposition is a requirement ~~of~~ for the orderly functioning of democratic government, so the existence of economic forces that resist institutional change may be necessary in order to keep the speed of this change within the limits of safety.

Now, one of the most powerful ~~of the~~ factors that make for acceleration of social change is inflation. ~~As~~ With so many authorities ~~have been~~ telling us that nothing undermines the framework of a society as does inflation, ~~that~~ it is hardly necessary to dwell upon this proposition. If we accept it, then it follows from what I have just said that from

all imaginable standpoints, the standpoint of irresponsible revolutionaries alone excepted, it is of prime importance after a war so to adjust a country's economic process as to stop it from producing further inflation. But it is clear at the same time that this is an extremely difficult thing to do in a world where everybody is afraid of the short-run consequences of such a policy and where some of the adjustments required--especially a rise in many previously controlled prices without a rise in money wage rates--is not "politically possible" at all.[3] The course that was the obvious one to take under the circumstances and that was actually followed after 1945--among mutual recriminations but still with a good deal of common consent--was to mitigate transitional difficulties by a dose of controlled peacetime inflation that was made more effective by the continuance of a high level of expenditure on the armed services and by the policy of European aid. Substantially, all this served its purpose and, as it became evident to most people though not to all economists, that a period of vigorous economic development, entailing vast investment requirements, was at hand, the hope that major disturbances would be avoided and that the economy of the ~~U.S.~~ United States would expand on a slowly rising price level was, for a time, not altogether unreasonable--whatever, short of another world war, might happen abroad.

Considerations of this type fail, however, to take into account an ominous fact. At a high level of employment (we seem, at long last, to be abandoning full-employment slogans)--whether "natural" or enforced by high-employment policies, wages demands or other demands that increase the money cost of employing labor become both inevitable and inflationary.

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[3] The alternative course, scaling down other prices and money wages, is not only still less "politically possible" but also much more difficult to do without causing a serious depression.

They become inevitable because high-level employment removes the only reason why they should not be raised. And they become inflationary because, with high utilization of resources, borrowing from banks and upward revision of prices provides a perfectly easy method--~~but at the same time the only method--~~of satisfying them. Though bargaining is still with individual trade unions, the movement is really a general one; so that we are drifting into the Keynesian situation in which the money wage rate no longer affects output and employment but only the value of the monetary unit. The situations of trade-union leadership and of government being what they are, there is nothing to stop this mechanism which--barring exceptions that are due to the particular situations of certain firms--spells perennial inflationary pressure. Rising demands upon the Treasury and our hyper-progressive methods of taxation aggravate this condition, of course, but they have not created it.

There should be no need to state that breaks in prices such as have occurred and will occur again prove nothing against the presence of inflationary pressure. Even apart from the postwar movements of agricultural prices and other self-explanatory cases, such breaks occur characteristically in the course of every inflation--as could be nicely illustrated from the German inflation that followed upon the first world war. People who are "caught," then cry out about deflation, and so do those fellow economists of ours who have deflationary prognoses to live down and who, in any case, seem incapable of foreseeing anything but deflation. But it is a compliment, the more sincere because unintentional, to the productive powers of American industry that doubts are at all possible as to whether our society is menaced by inflation or deflation.

III

A state of perennial inflationary pressure will have, qualitatively, all the effects of weakening the social framework of society and of strengthening subversive tendencies (however carefully wrapped up in "liberal" phrases) that every competent economist is in the habit of attributing to more spectacular inflations. But this is not all. In addition, some of the standard remedies for such situations will not mitigate, and may even aggravate, the present one. It seems to me that this is not being fully understood. Let us, therefore, in desperate brevity, discuss three types of such remedies.

(a) The most orthodox of all measures for the control of inflation is action upon the volume of borrowing through interest rates or credit rationing and the like. I fully understand, of course, that money rates must be freed from the grip of cheap-money policies if normalcy in the sense of a free-enterprise economy is to be attained, and that for everyone who desires return to such normalcy, the liberation--or reconstruction--of a free-money market must be a point of prime importance. But this does not alter the fact that a restrictive credit policy would at present produce consequences quite different from those that the old theory of credit policy would lead us to expect. Accepting the latter without any qualification--for argument's sake--we cannot help observing that it was, to apply to a world in which everything was entirely ~~feasible~~ flexible, and which was not afraid of what I may term remedial recessions. In such a world, an increase in interest rates was supposed to reduce the volume of operations, money wages, and employment. Surely these effects would not materialize at present and, if they did, they would immediately provoke

government action to neutralize them. In other words, credit restrictions would at present achieve little beyond increasing the difficulties of business. Even restrictions of consumers' credit would have this effect to some extent, though something could no doubt be done in this field.

(b) Similar difficulties stand in the way of controlling inflation by means of increasing taxation--a no less orthodox remedy but which enjoys a popularity with modern economists that is denied to credit restriction. It is quite true that something might be accomplished by increasing taxes on consumption. In an inflationary situation this would even be good Keynesianism. But if it is the corporation tax and the higher-bracket income tax which is to be increased, the effect upon inflationary pressure would be small at best and might even be negative. For if the present rate of industrial progress is to continue and therefore the present rate of obsolescence of equipment is to continue, also, ~~correspondingly~~ increasing resort would have to be taken to inflationary bank credit in order to make up for the decrease in the available ~~means of~~ non-inflationary means of finance. Alternatively, a decrease in those rates of progress and of obsolescence, would indeed decrease inflationary pressure for the moment but increase it in the long run.*

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* I have no difficulty in understanding why this argument does not impress our radical friends. But I confess that I find it difficult to understand the position of some excellent economists who are quite above any suspicion ~~to the effect~~ that they would welcome ~~any~~ the failure of our industrial engine to work on successfully and who nevertheless list reduction in industrial investment among the acceptable means for counteracting inflation, both in this country and in England. Incidentally, it should be noticed that the opinion of some conservative stalwarts that high and highly progressive taxation might promote, and that reductions in taxation (at the right spots) might decrease inflationary dangers, does not necessarily merit all the sneers it usually gets.

(c) The third household remedy consists in direct controls: price fixing, priorities and the like, including subsidies. Why they are so popular with certain sectors of public opinion is a question that need not concern us; for the bureaucracy in particular their reintroduction would spell reconquest of ground that has been lost; for the trade unions it would spell a decisive advantage in the campaign for the conquest of the profit item; for business it would mean the loss of the line of retreat that is open to it so long as most, if not all, attacks upon it can be, partly, if not wholly, parried by price adjustments; or at least, it would make this retreat dependent upon government permission, which there is no reason to believe would be granted for purposes of securing means for improving the productive engine. In other words, price control may result in a surrender of private enterprise to public authority; that is, in a big stride toward the perfectly planned economy.

8/8 reduce

[At this point Joseph Schumpeter stopped in the writing up of his notes. Those who heard the address will remember that at the end, there was little time and he summed up very briefly, going back to his opening remarks on the relevance, for the economic future of this country, of the present state of inflationary pressure, under existing political conditions. Some of the points touched upon with "desperate brevity" may be found developed at greater length in the second American edition or in the third English edition of Capitalism, Socialism and Democracy and in an article, "There is Still Time to Stop Inflation," which appeared in the Nation's Business for June, 1948.
The following paragraphs are reconstructed from memory and from the notes used for the address].

I do not pretend to prophecy; I merely recognize the facts and point out the tendencies which those facts indicate.

Perennial inflationary pressure can play an important part in the eventual conquest of the private-enterprise system by the bureaucracy ~~with~~ the resultant frictions and deadlocks being attributed to private enterprise and used as arguments for further restrictions and regulations. I do not say that any group follows this line with conscious purpose, but purposes are never wholly conscious. A situation may well emerge in which most people will consider complete planning as the smallest of possible evils. They will certainly not call it socialism or communism, and they will presumably make some exceptions for the farmer, the retailer, and the small producer; under these circumstances, the free-enterprise system as a scheme of values, a way of life, and a civilization may not be worth bothering about.

Whether the American genius for mass production on whose past performance all optimism for this way of life rests, is up to this test, I dare not affirm, nor do I dare to affirm that

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the policies responsible for this situation might be reversed.

Marx was wrong in his diagnosis of the manner in which capitalist society would break down; he was not wrong in the prediction that it would break down eventually. The stagnationists are wrong in their diagnosis of the reasons why the capitalist process should stagnate; they may still turn out to be right in their prognosis that it will stagnate—with sufficient help from the public sector.

Send proofs to
Mrs. J. A. Schumpeter
7 Acacia St
Cambridge 38
Mass.

Notes found on desk, day of death

10/29/2015

M-G

Lyncus

S.

E.B.

Cochrane

4

Notes found on desk, day of

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Single Space

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The following paragraphs are reconstructed from memory and from the notes used for the address]

Space.

Double Space.

I do not pretend to prophecy; I merely recognize the facts and point out the tendencies which those facts indicate. ¶ Perennial inflationary pressure can play an important part in the eventual conquest of the private-enterprise system by the ~~bracracracy~~ bureaucracy with the resultant

1b.

Joseph Schumpeter delivered his address The March into Socialism before the American Economic Association in New York on December 30, 1949 from notes and not from a prepared manuscript. He was writing up these notes for the Proceedings and had all but finished his paper the evening before his death. He expected to complete it the next day (January 8, 1950) before leaving for Chicago to deliver the Walgreen Foundation Lectures. The paper is a first draft but carefully written in his own hand, as were all his writings; there was no opportunity for him to make minor corrections or to write the concluding paragraphs. The corrections which consist largely in supplying punctuation or an occasional missing word have been kept to a minimum. The brief concluding paragraphs have been supplied by his wife from notes and memory.

Notes found on desk, day of S.'s death, unfinished MS of "The March into Socialism"

~~Bubbleson~~ Galley 21

page 5. of J.A.S. notes for address "The Marching into Socialism"

Conquest of bureaucracy of private enterprise (— via credit —); friction; deadlock; attributed to private enterprise.

I do not say that any group follows this line as conscious purpose; — and yet purposes never wholly conscious

I do say that a situation may emerge in which most people may consider complete planning as the smallest of possible evils

They will certainly not call it Socialism or Communism and they will presumably make some exceptions for the farmer, retailer and small producer

But the free enterprise system is ---- mere ceremonial ---- as a way of life may not be worth bothering about.

Whether the American genius for mass — in whose past performance all optimism for this way of life rests, is up to this task, I dare not affirm, nor do I dare to affirm that the policies responsible for this situation might be reversed

Marx was wrong in his diagnosis of the manner in which capitalist society would break down; he was not wrong in the prediction that it would break down eventually.

Stagnationists are wrong in their diagnosis of the reasons why the capitalist process should stagnate. They may still turn out to be right in their prognosis that it would well must stagnate — with sufficient help from the public sector

Feb 1, 2 or 3

Julia –

Scott

Mrs Scott. Time Life Fortune.

Marching into Socialism

page 10

Page 14 Note referring to article in nations business.

Notes found on desk, day of J.'s death, among

METROPOLITAN LIFE INSURANCE COMPANY
ONE MADISON AVENUE, NEW YORK 10, N.Y.

January 12, 1950

WILLIAM A. BERRIDGE
ECONOMIST

Mrs. Joseph A. Schumpeter
Taconic
Connecticut

Dear Lizzie:

As agreed on Tuesday, I have looked up the notes made by the two Bureau assistants who heard Joe's "March into Socialism" address of December 30, Misses Margaret Coffman & Mary Morris.

It seems better to leave them in the form of direct and independent eye-witness accounts. Various cross-collatings of thought and language between these (and other) versions can far better be done by you. However, I take the liberty of adding the following remarks by Ruth, who had the advantage of hearing the entire address, though she took no notes. These remarks or insertions pertain to the corresponding numerals marked in red on Miss Morris' notes:*

(I myself heard only the last third or half.)

1 Because (a) he does not know what is meant by "undesirable" and (b) he does not claim that trends will inevitably reach their logical consequences.

2 Which he said are the same.

3 His grounds for predicting the trend toward Socialism are (a) ideological (our egalitarianism) and (b) our inflationary pressures (see further on in typed notes).

4 R.R.B. thinks he said 1914, not 1919.

We all hope these materials will help you reconstruct the text for publication.

With cordial sympathy and regards, I remain

Faithfully yours,

WAB.

* (Of the two Bureau assistants, Miss Morris is the stenographer but had been asked to note down only the gist, so that even her version cannot at any point be considered a verbatim.)

B

P.S. These ladies remind me of this godsend: That Joe's A.E.A. meeting, unlike any that I can recall, had associated with it an official listed as "Rapporteur: Maxwell Obst, N.Y.C." We are unable to identify or locate him readily but thought you yourself would wish to communicate with Jim Bell concerning him, or perhaps have even done so already.

notes by Miss Margaret A. Coffman

Notes found on desk,

The March into Socialism

by Joseph A. Schumpeter, Harvard University

In the field of Economics, it is difficult to separate wishful thinking from predictions. It must be kept in mind that nothing is inevitable. Professor Schumpeter is reporting facts as he sees them, and from these facts deducting tendencies. But it is not necessary that these tendencies will reach their logical conclusions.

Professor Schumpeter disagrees that socialism is inevitable or undesirable. He defines socialism which he sees developing in the U.S. as a state in which the central authority governs all of the means of production. Any socialism or communism in the U.S. will be in fact, never in name, and it is likely to fall short of agrarian socialism because of America's ideal of the farm life.

In the U.S. there is a general tendency towards central socialism as a natural consequence of the capitalistic society. There could develop a guild socialism, stemming from labor union power, or an [redacted], which is likely only in a Catholic country. The latter form is preferable but knowledge of this form is almost nonexistent in non catholic countries.

Instability and inequality are basic in the capitalistic economy. The predictions of Karl Marx failed because he failed to see that capitalism would be championed by the working man.

Today there is wide distrust of the profits motive, but there is strong belief that a man should have the ability to finance himself.

The long time trend is slow; it can be retarded or hastened by chance occurences, the most important of which is total war. During a total war new classes of people are formed, and of these the most important are the public servants. These people become a power organ of which one of its smallest powers is its weight at the polls.

The capitalistic economies of Europe were clashing before 1914, and World War I only emphasized this. After the war the socialist party came into power in Germany. This is what Marx had failed to foresee, that capitalism would turn to labor for protection.

Inflation will continue. Today there is the large armaments program, the G.I. benefits, large payments as gifts to foreigners, and an almost limitless expansion of grants for social services. Since the time of Roosevelt, the public section has been increasingly wasteful seemingly holding the belief that spending is good per se. The Hoover Commission was set up to correct this, but Professor Schumpeter has inferred that little will be done. The high employment and wage policy is also inflationary, and this will make it impossible to have a correction. Also adding to this are the government's cheap money policy and the anti-trust policy. So the economy is faced with perennial inflationary pressure although this may be interrupted by intermissions which will look like deflation. And the other socialistic tendencies probably also will experience similar intermissions.

The public section of our economy has probably always been wasteful.

Remedies that probably will be called for by the public are (1) money and credit policy reform (but the old money market would have to be recreated and this would have an unfavorable effect on industry),

(2) taxation reform in order to balance the budget (but inflation can continue even with a balanced budget especially when there is full employment and other upward pressures), and (3) direct controls (but price control is followed by higher wage demands. This leads to a political deadlock, and it increases the tendency towards socialism.)

The socialistic creed is as good and as bad as any creed. Professor Schumpeter is not prophesying; he has facts to point out, and these facts show tendencies. It is entirely possible that American industrial genius will swamp these tendencies.

Political stagnation will help us into socialism as well as any other kind of stagnation.

PC
1/3

notes by Miss Mary F. Morris

Speech by Joseph A. Schumpeter, 12/30/49.

Schumpeter opened his speech with the statement that wishfulness and prediction are frequently one. Referring to the belief that Socialism is undesirable but inevitable, he vigorously disagrees with the thesis. (1)

Socialism and Communism, (2) if they come to America, will do so in fact but not in name. The American people instinctively shrink from the system that both these terms suggest. Schumpeter marvels at the loose fashion with which "wise" people throw around such vague terms as "Freedom," "Democracy," "Liberalism," etc., admitting that such words mean nothing to him.

The tendency of our working forces to participate in management, he thinks, is one of the deterring factors in our move toward Socialism. Should it come to this country, it would (might) be in the form of a guild rather than a centralized Socialism.

Schumpeter then refers to the papal encyclical "Quadragesimo Anno," declaring that its contents had been neglected and that it should receive more attention, although he feels this is not likely except in a country where the Catholic Church is politically powerful. Following its recommendations, he said, would: (1) avoid an all powerful State, (2) produce a democratically organized industrial setup.

Schumpeter declares that dislike of the word "capitalism," is a characteristic of all good economists. (3) Large numbers of us accept a large amount of egalitarianism. Stabilization is now an end in itself. Nevertheless, instability and inequality are characteristic of our civilization.

Fortunately, he states, we are getting away from the full employment idea -- thinking rather in terms of unemployment.

Karl Marx failed to see the possibilities of the free enterprise system. He was in favor of a system ruled exclusively by the working people.

We have already left the capitalist scheme and can't go back -- we are far from the capitalism of 100 years ago. Labor and the money market have gone from private to the public sphere. It is now under public administration. Some profit incentive may have its place here, but that isn't capitalism. . We don't argue for it on principle.

* * * *

The theory of social process involves an investigation of certain factors which produce a long term trend. These factors work slowly and quietly but can be accelerated by events such as wars.

Marx also did not foresee that businessmen would turn to the labor class for protection. (4)

"Merrie England" died in ~~1919~~ 1914 -- although Schumpeter himself believes the date might be set as early as 1906.

A situation unfavorable to the survival of capitalism and favorable to the organization of society is accelerated by persistent inflationary pressures. Total wars create new classes of public administrators, bringing long suffering citizens to accept the dictates of Government. This is one of the smallest of the sources of power. However, it is only one side and raises no problem in the scientific sense.

In addition, we have now in this country a perennial inflationary force. (Some even say we are, at present, in a deflationary period.) Inflationary pressure will go on for the following reasons:

(1) Indefinitely large disarmament program.

(2) An indefinitely long program of gratis payments before us. The awakening of the citizens will make politicians more cautious, but will not change the fundamental arrangement. They will merely use another term such as grant or loan, but it will be just a euphemism for the same thing.

(3) An almost limitless expanse of plans for social service which we might agree with, but which will, nevertheless, create a serious problem. Education, hygiene -- these are just chicken feed -- others yet to come will create a tremendous drain on the Treasury.

(4) Our public sector is wasteful on principle. It was wasteful before Roosevelt because the administrators couldn't help it. Since then waste has become a virtue -- a remedial measure. Schumpeter says that little will be done about the Hoover Commission.

(5) Inflationary pressure is inevitable with our wage policy during a high employment period. This situation prevents the maintenance of a compensation cushion for upsurges in prices from time to time.

(6) The cheap money policy and the handling of the antitrust policy.

Schumpeter declares that there is no economic progress without monopoly -- that there are inflationary intermissions which look like depressions. These inflationary pressures per se, he believes, could be enough to undermine our capitalistic society.

* * * *

He suggests the following remedies:

(1) Regarding money and credit policies, a rebuilding of interest rates is in order. This will be necessary in the long run. If the old meaning of money market were reconstructed now, it might be as unfavorable on production as it is favorable now on output. (?)

(2) Regarding taxation and a balanced budget, it is not sufficient for the public sector to exert a good influence. Taxation could be levied in such a way as to stop production in a year. A balanced budget could even be an <u>inflationary</u> pressure too, though.

(3) The direct control of prices will force the surrender of private industries -- high wages coupled with inability to raise prices would conspire to bring this about. In this way a political condition would create an economic stalemate and could lead to Socialism.

As for the outlook, Schumpeter does not pretend to prophesy; he merely recognizes facts and shows the tendencies which they indicate. He states that the tremendous efficiency of American industry may swamp all these things, but feels that its action would have to be ingenious to do so. Declaring that he agrees with neither the arguments of stagnation nor those of Karl Marx, he states, nevertheless, that there is such a thing as a politically induced stagnation and such a thing could lead us to Socialism.

Note: S.'s death left the manuscript unfinished

Not much good! Was in Gad form

MARX AND MILL

For an historian of economic thought, few tasks can be more attractive than to compare the types of mind, the work, the lives of Marx and Mill. Though Nature had cast them into such different molds there are affinities between them which it is most instructive to bring out. They were both typical 19th century intellectuals with their roots in the 18th century and it was external circumstances only that formed the one into a respectable employee of the India Company and the other into a wrathful prophet, or if you prefer, ranting demagogue. Leaving out the foaming oratory of the latter, the similarities come into view.

This applies first to their philosophical background. It is true that Marx was a Hegalian and that he affected to hate and despise Bentham; it is also true that Mill in the course of his life drew far away from his early Benthamite moorings, under Comtist Sainte-Simoniste and even Carlylian influence, but the essential thing is that both Mill and Marx were perhaps primarily, certainly to a very great extent, philosophers. Marx originally contemplated the career of a pacific German professor of philosophy. Mill wrote his most elaborate and in fact most finished great work in that field, namely the Discussion of Hamilton's Philosophy. In the end, their path in that field, however, converged. They both emerged as something like modern positivists, equally opposed to anything like metaphysics and equally distrustful of the visionary, the emotional, the non-

observable.

This philosophical background produced political philosophies that have much more in common than appears on the surfaces; if we discount Marx's glowing phrases about revolution, spectacular breakdowns and so on, we find very much more of the bourgeois radical than Marx would have liked to admit. In order to satisfy ourselves of this we have only to read the political program near the end of the Communist Manifesto, which, largely realized by now, was just the political program current among bourgeois radicals 100 years ago. Mill, on the other hand, was from an early age and to the end an evolutionary socialist of the associationist type. Certainly he did not believe in violent change and no less certainly he was a pacific and law-abiding citizen and a very respectable man. He never hesitated to speak the truth about disagreeable facts and he faced difficulties with an honesty that makes him in this, as he is in other respects, a paragon. But behind all this there is first the conviction evident from his correspondence with Comte and also from his Principles that the Private Enterprise Society is an historical phase that is about to develop into something else. The Associationism came to him mainly from the French socialists, especially Fourier and Louis Blanc, less from St-Simon. He visualized the future social organization not, as did Marx, in the form of Centralist-Socialism but in a form that is more akin to Guild Socialism, namely as an agglomeration of workers' productive associations in which workers would own the means of production. Secondly, therefore, he believed as did Marx in

the ability of the working class to solve the problems of modern production without being disciplined and guided by non-proletarian elements and this in turn implies that he believed, as is particularly evident from a letter of his to Lord Durham, in the fundamental equality of human nature in all social strata and races, a human nature that is moulded into different types by education and other environmental influences--a view which, by the way, was also sponsored by Adam Smith.

It is of particular interest, however, that the technical economics of both men do not differ as much as Marx wanted his readers to believe. Nor is this surprising since the purely analytical roots of both are in the work of Ricardo. Marx, so it seems, not only learned his economics from Ricardo, but he accepted his theoretical scheme and all theoretical problems presented themselves to Marx in the form which Ricardo had given them. For instance in the theory of value, Marx elaborated the leading idea of the labor-quantity theory. He observed how Ricardo met the fact that prices of commodities are actually not proportional to the labor-time embodied in these commodities. Ricardo endeavoured to uphold his labor quantity law at least as an approximation and for the rest admitted that the time element causes a systematic deviation from it. Marx was dissatisfied with this, but his theory of surplus value is nothing else but an attempt to solve the problem as presented by Ricardo, though in a way that differed from Ricardo's. Another example of the parallelism between both theoretical structures is Marx's theory of the "reserve army",

that is to say of permanent unemployment; this unemployment was not Keynesian unemployment but exclusively technological; ~~but~~ it was due to the setting free of labor by the introduction of labor-saving machinery. This was quite essential to Marx's system because the presence of this "army" was the fundamental factor that pressed upon the workmen's standard of life and thus supported the theory of increasing misery, Marx's most infelicitous prediction. Now this theory of technological unemployment is entirely taken from Chapter 31 of Ricardo's Principles that was ~~published~~, under the influence of Barton, introduced in the third edition. ~~Moreover,~~ John Stuart Mill had the same training but he developed both the Ricardian theories of value and of technological unemployment in a different way, mainly under the influence of Jean Baptiste Say and of Senior. The dilemma which arises from the fact that values are not proportional to labor embodied he resolved by the introduction of Senior's theory of abstinence and the technological unemployment he allowed to be drowned by the effects of quick accumulation that would always leave a surplus of sufficient amounts for the ~~incomes~~ increase of the wage fund even if part of the accumulation went into fixed capital. On analysis of the two arguments we realize that Marx ought to have admitted this, but he was debarred from doing so by the key position which in his social vision was held by the element of increasing misery. Thus Mill arrived at the very much more realistic prediction which he expressed by saying that there was no reason for looking upon the future of the working classes as "otherwise than hopeful". There is another field in which parallelisms stand out strikingly, the field of money and credit. It is true that Marx renounced the quantity theory of money very much more energetically than Mill, who allowed it

to stand ~~for~~ in an entirely impractical primitive case, but in the result, Marx's and Mill's theory of money and credit do not greatly differ and this is again due to the fact that they were both under the influence of the same teaching, in this case, Tooke's and Fullarton's.