14.72
More Review

liberalism → liberty + equality

Classical liberalism → Civil liberties, political freedom

Friedman

Neo-classical liberalism → gov as small as possible

aka **neoliberal**

(makes more sense now!)

aka **libertarism** – small gov
just protects from violence
+ private property

or economically conservative + socially liberal

fiscal conservatism ↓ gov spending
balence budget

So really liberalism + conservatism not all that different!
yellow flag blue flag

(2)

<u>Social liberalism</u> ~~R~~ role of state includes welfare,
~~hed~~ health care, education
while expanding civil + political rights

good of community <u>and</u> right of individual

aka <u>modern liberalism</u>

inc Keynes + ~~K~~ Krugman + Rawls
"liberal" today ∋ modern liberalism

New Deal + Great Society
Social justice

(reading about Great Society CAPs)

(3)

Progressivism - wanting reform

often means modern liberalism

Communism - Classless, moneyless, stateless

Common ownership of means of productions

Socialism - social ownership of means of production

political philosophy advocating this

facism - radical authoritarian nationalist political ideology

ancestry + culture

totalitarianism - state has total authority

Authoritarian - submission to authority

usually a small group of politicians

(4)

totalitarianism is extream version of authoritarianism
more overall control

State planning economic system where decisions
made by gov agency
Think it better allows for perfect info
nope

I wonder what management methods they
used and how sophisticated they were

How would you ideally structure such an org?
~~Ideally~~ (still not better than capitalism)
Saudi Arabia
So Chile tried w/ Project Cybersyn
Cybernetics
had fancy control rooms w/ 60s/70s chairs
for creativity :)

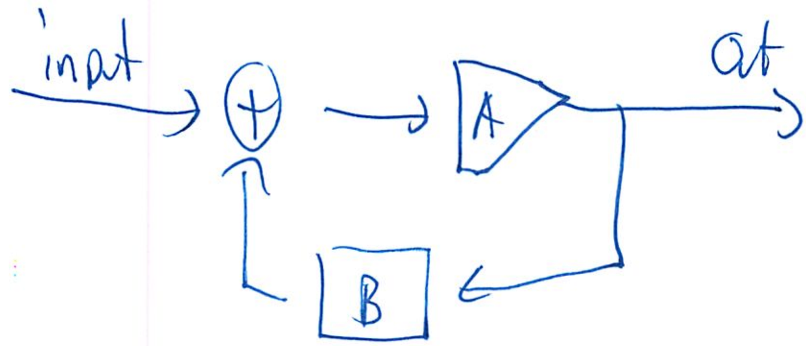
5

(¿Does my creativity change depending on how I sat?)

Cybernetics transdisciplinary approach for exploring regulatory systems, their structures, constraints, + probabilities

Closed ~~[illegible]~~ signal loop

like system dynamics



System dynamics - understanding complex systems over time

Uses feedback loops + time delays

~~[illegible]~~ even simple systems non linear

(this stuff is interesting, I wish I could learn more)

6

<u>kleptocracy</u> rule by themselves

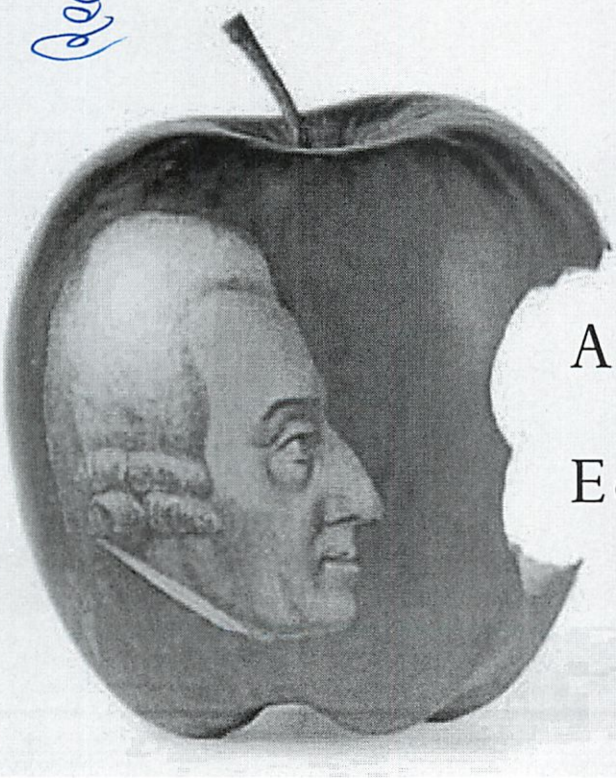
gov increases personal wealth at top

often w/o pretense of honest service

Adam's Fallacy

Read 10/20 late

DUNCAN K. FOLEY



A Guide to Economic Theology

14.72 10/22

Social Embeddedness
of Economy Intro

Exams + Papers back Wed
Vincent graded
Will explain solutions

Pos + Neg freedom
Issach Berlin
diff b/w Ayn Rand + - must realise yourself
Milton freedom − - don't constrain someone

Plato
Marx - about + freedom
market gives plenty −
but then what is + freedom worth?

②

Today: New Paradigms

Sociological or Antropological

Diff world

3 things

1. Protestent Ethic - Max Webber "Vay-bar"

2. Polani

had to summarize

3. Shumpeter

econ + sociology

Keynes - controversal

Transition class

Some pieces of Marx lead towards this

Did miss a class on Marxism

(3)

Marx Central argument

Speestructure
- culture
- government
- art
- architecture

Base
- tech
- Social relation of protection (Classes)

Big break → revolution

Causality

Superstructure
↑
Base

But Marx didn't really fit the world

Tried to adopt Marx to world

Where did Marx go wrong?

Technology didn't go the way he emphasized

Only realize otherwise in 80s + 90s

- larger firms
- deskilling
- Centralization

But no revolution

was class conflict kinda

(9)

didn't happen where supposed to
└ industrial society
happened where not supposed to
└ Russia + China
└ pre industrial society

4 Categories
Colonialism - development of colonial theory
Rosa Luxemberg
as capitalists ~~get~~ need to grow profits - need to exploit labor more
Spreads capitalists more
reproduction of class conflict
dev vs developing world

Lenism - revolution would not just happen
had to be made
Someone must lead
Communist Party
Needs a letter

5

Lenin: revolution ~~inevitable~~ impossible w/o strong leadership

So 2nd big change in Communism in 20th Century

~~Didn't~~ Not the case: Don't do anything, rev will happen

Role of Government

3 diff camps for Role of Gov

1. Communist Manifesto: Instrumental View

Gov is just exec committe of ruling class

Direct reflection of ruling class on gov

~~Gov~~ Gov just persues interest of ruling class

Assumes ruling class has unified interest

Simple ~~state~~ view Superstructure ↑ Base

So just understand ruling class

(6)

2. Structural View Not just mapping base onto superstructure

Any gov that wants to survive must do certain things

European Austerity programs

Since Markets forcing onto them

1970 French Socialist Gov

investment left country

$ fleed

reversed 1982

3. Historic Marxism

no unified ruling class

Sometimes ruling class unified

in early + middle capitalism

each industry has a diff interest

7

But esp since no single ruling class

Bain Capital - is capitalist

~~[illegible]~~ makes $ anywhere

no sense of identity

50s + 60s → each industry had own identity

People/cos didn't change industry

Diff ruling classes

So can't just look at class conflict

But often gov has polices that might not be interest of ruling class but help ruling class

- Social Security

but saved capitalism

gov became autonomous actor

(8)

1. No need for model of how gov operates

2+3. → gov has a certain autonomy

So why do you have ~~[illegible]~~ rev when ~~sup~~ not supposed to

↳ Antonio Gramsci (Italy)
(missed

Country economically exausted from war

Forced treaty w/ Germany

Russians thought rev would happen elsewhere

Street demonstrations now

looked not like Greece, ~~[illegible]~~ but Syria

looked like Communists might take over

Germany + Italy + Spain

early 20s

proto civil war

but who in the end took over?

facsits - the right wing, not left wing!

9

Supposed to be communist

But facisest

Facism dictatorship

supported by biz classes + right wing

but state has a lot of autonomy

also a lot of support from small biz + pesants

not just power, but philosophy

Worker councils rising up + taking over industries

- Soviets ← where term came from

(10)

Italian communitsts
Coded messages in jail

Gramsci → revolution in underdeveloped countries
Since philosophy of Communism underdeveloped
Just need to take over Winter Palace

Russia → took over Tsar
nothing else there except Police + Army
So that explains Russian Rev

Then ~~Communism~~ Capitalism → ideological aperatus
that protects capitalism
Can only win rev by overcoming ideological bias
w/ alt way of looking at the world

1. Must Make Rev
like Lenin

Need a way to over take ideology of capitalism

(21)

But what is the dominant ideology today?

What protects capitalism today?

- a set of values?
  - private property
  - liberty
- if value these things & obstacles to those

(Ted's digression on Chrysler bondholders)

went to unions

? unions have lost clout?

~~people~~ diff property + money

? sell property for $

can sell yourself into slavery?

indentured servants

Prof ways of making private property generic

defined by law

(12)

1930s Europe

Communism + Facism

↑ spread 2nd ↑ ~~the~~ spread 1st

Prof: Europe is falling apart now

Catalonia might withdraw from Spain

People furious

but no one talking of communism + facism

Perhaps nationalism

(US is very nationalist - but not fascist)

Communist + Fascist have ~~had~~ been discredited

Prof: You can't imagine any alt to market

Gramsci: People don't like market

Can't image alt

↳ intellectual hegemity

13

Must imagine ~~diff~~ diff system and think its possible

~~So back~~ :

Gramsci : Neoliberalism is preventing revolution

~~Value of private pa~~

don't see an alt way

except through private property + market

Led to communist party in ~~I~~ Italy ~~a~~ that is

seeking ~~the~~ intellectual revolution

~1930s

Communists strong at end WW2

But then wanted to win through election

True until 1980s

When Russia fell

+ Communism completly discreted

Split into right-wing + left-wing Communism

└ Miteran / market

(14)

Keynes: Ideas dominate everything
If want to change world,
need new set of ideas

Right wing vs left wing
Concern for income dist, poverty,
socially stigmatized group

Once give up alt system proposal its hard to
distinguish the two

Since everyone in US wants a market economy

Gramsci: nothing about values
instead intellectual ~~[illegible]~~ conception
must concieve of system w/o private property

15

Ted: How to incentive people?

Prof: Protistent Ethic + Spirit of Capitalism

As you read it, think about that qu

Protisterism brings about capitalism

~~Nat~~ kinda something to do w/ people being lazy

Used to be everyone was a Protistant
at MIT

Webber: Specifically Calvism - pre destination

nothing you can do in life can change

and yet this led people to be motivated to be super Capitalists

not at all lazy

ideas ruled the world

16

If Protestism is not really around?
why is everyone a capitalist now

Ted: Some incentive to work hard to be part of "elect"

Rand wrote about productivity creativity for its own sake

Prof: plenty of alts. Focus on this one

Mind driving stuff is central feature

Marx + Liberalism againts that

↓ ↓ external ↓ world

technology ↙ ↘ scarcity

This is like theocracy

So set up againts both

ideas / in head drives stuff

The Protestant Ethic and the Spirit of Capitalism

From Wikipedia, the free encyclopedia

Read 10/29

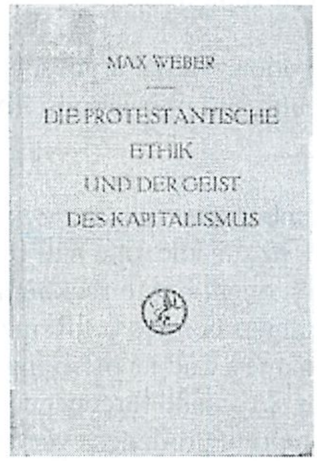
The Protestant Ethic and the Spirit of Capitalism is a book written by Max Weber, a German sociologist, economist, and politician. Begun as a series of essays, the original German text was composed in 1904 and 1905, and was translated into English for the first time by Talcott Parsons in 1930.[1] It is considered a founding text in economic sociology and sociology in general.

Oh

In the book, Weber wrote that capitalism in northern Europe evolved when the Protestant (particularly Calvinist) ethic influenced large numbers of people to engage in work in the secular world, developing their own enterprises and engaging in trade and the accumulation of wealth for investment. In other words, the Protestant work ethic was an important force behind the unplanned and uncoordinated mass action that influenced the development of capitalism. This idea is also known as the "Protestant Ethic thesis."[2]

In 1998 the International Sociological Association listed this work as the fourth most important sociological book of the 20th century.[3]

The Protestant Ethic and the Spirit of Capitalism



Cover of the German edition from 1934

Author(s)	Max Weber
Country	Germany
Language	German
Publication date	1905

Contents

Summary

Basic concepts

Although not a detailed study of Protestantism but rather an introduction to Weber's later studies of interaction between various religious ideas and economics (*The Religion of China: Confucianism and Taoism, The Religion of India: The Sociology of Hinduism and Buddhism,* and *Ancient Judaism*), *The Protestant Ethic and the Spirit of Capitalism* argues that Puritan ethics and ideas influenced the development of capitalism.

Religious devotion, Weber argues, is usually accompanied by a rejection of worldly affairs, including the pursuit of wealth and possessions. To illustrate his theory, Weber quotes the ethical writings of Benjamin Franklin:

> "Remember, that *time is money*. He that can earn ten shillings a day by his labor, and goes abroad, or sits idle, one half of that day, though he spends but sixpence during his diversion or idleness, ought not to reckon *that* the only expense; he has really spent, or rather thrown away, five shillings besides.[...]Remember, that money is the *prolific, generating nature*. Money can beget money, and its offspring can beget more, and so on. Five shillings turned is six, turned again is seven and threepence, and so on, till it becomes a hundred pounds. The more there is of it, the more it produces every turning, so that the profits rise quicker and quicker. He that kills a breeding sow, destroys all her offspring to the thousandth generation. He that murders a crown, destroys all that it might have produced, even scores of pounds.

Weber notes that this is not a philosophy of mere greed, but a statement laden with moral language. Indeed, Franklin claims that God revealed the usefulness of virtue to him.[4]:9–12

The Reformation profoundly affected the view of work, dignifying even the most mundane professions as adding to the common good and thus blessed by God, as much as any "sacred" calling. A common illustration is that of a cobbler, hunched over his work, who devotes his entire effort to the praise of God.

To emphasize the work ethic in Protestantism relative to Catholics, he notes a common problem that industrialists face when employing precapitalist laborers: Agricultural entrepreneurs will try to encourage time spent harvesting by offering a higher wage, with the expectation that laborers will see time spent working as more valuable and so engage it longer. However, in precapitalist societies this often results in laborers spending *less* time harvesting. Laborers judge that they can earn the same, while spending less time working and having more leisure. He also notes that societies having more Protestants are those that have a more developed capitalist economy.[4]:15–16

It is particularly advantageous in technical occupations for workers to be extremely devoted to their craft. To view the craft as an end in itself, or as a "calling" would serve this need well. This attitude is well-noted in certain classes which have endured religious education, especially of a Pietist background.[4]:17

He defines spirit of capitalism as the ideas and *esprit* that favour the rational pursuit of economic gain: "We shall nevertheless provisionally use the expression 'spirit of capitalism' for that attitude which, *in the pursuit of a calling [berufsmäßig]*, strives systematically for profit for its own sake in the manner exemplified by Benjamin Franklin."[4]:19

Weber points out that such a spirit is not limited to Western culture if one considers it as the attitude of individuals, but that such individuals – heroic entrepreneurs, as he calls them – could not by themselves establish a new economic order (capitalism).[5]:54–55 He further noted that the spirit of capitalism could be divorced from religion, and that those passionate capitalists of his era were either passionate against the ~~Church or at least~~ indifferent to it.[4]:23 Desire for profit with minimum effort and seeing work as a burden to be avoided, and doing no more than what was enough for modest life, were common attitudes.[5]:55 As he wrote in his essays:

> In order that a manner of life well adapted to the peculiarities of the capitalism… could come to dominate others, it had to originate somewhere, and not in isolated individuals alone, but as a way of life common to the whole groups of man.

After defining the "spirit of capitalism," Weber argues that there are many reasons to find its origins in the religious ideas of the Reformation. Many others like William Petty, Montesquieu, Henry Thomas Buckle, John Keats have noted the affinity between Protestantism and the development of commercialism.[6]

Weber shows that certain branches of Protestantism had supported worldly activities dedicated to economic gain, seeing them as endowed with moral and spiritual significance. This recognition was not a goal in itself; rather they were a byproduct of other doctrines of faith that encouraged planning, hard work and self-denial in the pursuit of worldly riches.[5]:57

Origins of the Protestant work ethic

Weber traced the origins of the Protestant ethic to the Reformation, though he acknowledged some respect for secular everyday labor as early as the Middle Ages.[4]:28 The Roman Catholic Church assured salvation to individuals who accepted the church's sacraments and submitted to the clerical authority. However, the Reformation had effectively removed such assurances. From a psychological viewpoint, the average person had difficulty adjusting to this new worldview, and only the most devout believers or "religious geniuses" within Protestantism, such as Martin Luther, were able to make this adjustment, according to Weber.

In the absence of such assurances from religious authority, Weber argued that Protestants began to look for other "signs" that they were saved. Calvin and his followers taught a doctrine of double predestination, in which from the beginning God chose some people for salvation and others for damnation. The inability to influence one's own salvation presented a very difficult problem for Calvin's followers. It became an absolute duty to believe that one was chosen for salvation, and to dispel any doubt about that: lack of self-confidence was evidence of insufficient faith and a sign of damnation. So, self-confidence took the place of priestly assurance of God's grace.

Worldly success became one measure of that self-confidence. Luther made an early endorsement of Europe's emerging labor divisions. Weber identifies the applicability of Luther's conclusions, noting that a "vocation" from God was no longer limited to the clergy or church, but applied to any occupation or trade.

However, Weber saw the fulfillment of the Protestant ethic not in Lutheranism, which was too concerned with the reception of divine spirit in the soul, but in Calvinistic forms of Christianity.[4]:32–33 The trend was carried further still in Pietism.[4]:90 The Baptists diluted the concept of the calling relative to Calvinists, but other aspects made its congregants fertile soil for the development of capitalism—namely, a lack of paralyzing ascetism, the refusal to accept state office and thereby develop *un*politically, and the doctrine of control by conscience which caused rigorous honesty.[4]:102–104

What Weber found, in simple terms:

- According to the new Protestant religions, an individual was religiously compelled to follow a secular vocation with as much zeal as possible. A person living according to this world view was more likely to accumulate money.
- The new religions (in particular, Calvinism and other more austere Protestant sects) effectively forbade wastefully *using* hard earned money and identified the purchase of luxuries as a sin. Donations to an individual's church or congregation were limited due to the rejection by certain Protestant sects of icons. Finally, donation of money to the poor or to charity was generally frowned on as it was seen as furthering beggary. This social condition was perceived as laziness, burdening their fellow man, and an affront to God; by not working, one failed to glorify God.

The manner in which this paradox was resolved, Weber argued, was the investment of this money, which gave an extreme boost to nascent capitalism.

The Protestant work ethic in Weber's time

By the time Weber wrote his essay, he believed that the religious underpinnings of the Protestant ethic had largely gone from society. He cited the writings of Benjamin Franklin, which emphasized frugality, hard work and thrift, but were mostly free of spiritual content. Weber also attributed the success of mass production partly to the Protestant ethic. Only after expensive luxuries were disdained, could individuals accept the uniform products, such as clothes and furniture, that industrialization offered.

In his remarkably prescient conclusion to the book, Weber lamented that the loss of religious underpinning to capitalism's spirit has led to a kind of involuntary servitude to mechanized industry.

> “ The Puritan wanted to work in calling; we are forced to do so. For when asceticism was carried out of monastic cells into everyday life, and began to dominate worldly morality, it did its part in building the tremendous cosmos of the modern economic order. This order is now bound to the technical and economic conditions of machine production which today determine the lives of all the individuals who are born into this mechanism, not only those directly concerned with economic acquisition, with irresistible force. Perhaps it will so determine them until the last ton of fossilized coal is burnt.In Baxter's view the care for external goods should only lie on the shoulders of the 'saint like a light cloak, which can be thrown aside at any moment.' But fate decreed that the cloak should become an iron cage. (Page 181, 1953 Scribner's edition.) ”

Weber maintained that while Puritan religious ideas had significantly impacted the development of economic system in Europe and United States, there were other factors in play, as well. They included the rationalism in scientific pursuit, growing connections between observation and mathematics, development of scholarship and jurisprudence, rational systematisation of government administration (development of bureaucracy) and advances in entrepreneurship. In the end, the study of Protestant ethic, according to Weber, investigated a part of the detachment from magic, that *disenchantment of the world* that could be seen as a unique characteristic of Western culture.[5]:60

Conclusions

In the final endnotes Weber states that he abandoned research into Protestantism because his colleague Ernst Troeltsch, a professional theologian, had begun work on *The Social Teachings of the Christian Churches and Sects*. Another reason for Weber's decision was that Troeltsch's work already achieved what he desired in that area, which is laying groundwork for comparative analysis of religion and society. Weber moved beyond Protestantism with his research but would continue research into sociology of religion within his later works (the study of Judaism and the religions of China and India).[5]:49

This book is also Weber's first brush with the concept of rationalization. His idea of modern capitalism as growing out of the religious pursuit of wealth meant a change to a rational means of existence, wealth. That is to say, at some point the Calvinist rationale informing the "spirit" of capitalism became unreliant on the underlying religious movement behind it, leaving only rational capitalism. In essence then, Weber's "Spirit of Capitalism" is effectively and more broadly a Spirit of Rationalization.

Reception

The essay can also be interpreted as one of Weber's criticisms of Karl Marx and his theories. While Marx's historical materialism held that all human institutions – including religion – were based on economic foundations, *The Protestant Ethic* turns this theory on its head by implying that a religious movement fostered capitalism, not the other way around.

Other scholars have taken a more nuanced view of Weber's argument. Weber states in the closing of this essay, "it is, of course, not my aim to substitute for a one-sided materialistic an equally one-sided spiritualistic causal interpretation of culture and history. Each is equally possible, but each if it does not serve as the preparation, but as the conclusion of an investigation, accomplishes equally little in the interest of historical truth." Weber's argument can be understood as an attempt to deepen the understanding of the cultural origins of capitalism, which does not exclude the historical materialist origins described by Marx.

Table of contents (from the 1958 Scribner's edition, translated by Talcott Parsons)

D. The Baptism Sects

Baptist and Quaker; Sect Principle; Inner Worldly Asceticism; Transformation of the World.

V. Asceticism and the Spirit of Capitalism

Richard Baxter; Meaning of Work; Justification of Profit; Jewish vs. Puritan Capitalism; Puritanism and Culture; Saving and Capital; Paradox of Asceticism and Rich; Serving Both Worlds; Citizenry Capitalistic Ethic; Iron Cage of Capitalism.

Criticisms

Economic criticism

The economist and historian Henryk Grossman criticises Weber's analysis on two fronts. Firstly with reference to Marx's extensive work which showed that the stringent legal measures taken against poverty and vagabondage was a reaction to the massive population shifts caused by the enclosure of the commons in England. And, secondly, in Grossman's own work showing how this "bloody legislation" against those who had been put off their land was effected across Europe and especially in France. For Grossman this legislation, the outlawing of idleness and the poorhouses they instituted physically forced people from serfdom into wage-labor. For him, this general fact was not related to protestantism and so capitalism came largely by force and not by any vocational training regarding an inner-worldliness of protestanism. Thus Grossman solves the central crux of Weber's analysis: his puzzlement over how enough people were recruited into early capitalist manufacturing. Grossman shows how people were in fact forced to obey capitalist principles not on any religious grounds but rather from legalistic grounds of force made by those who held power and wanted more production for their own benefit but also, often in their own view, for their nation's benefit.[7] However, it is possible that the Protestant "work ethic" reinforced or legitimized these legal measures within a larger cultural context.

In a paper published on 10 November 2009, Harvard economist Davide Cantoni tested Weber's Protestant hypothesis using population and economic growth in second-millennium Germany as the data set, with negative results. Cantoni writes:

> “Using population figures in a dataset comprising 276 cities in the years 1300–1900, I find no effects of Protestantism on economic growth. The finding is robust to the inclusion of a variety of controls, and does not appear to depend on data selection or small sample size. In addition, Protestantism has no effect when interacted with other likely determinants of economic development. I also analyze the endogeneity of religious choice; instrumental variables estimates of the effects of Protestantism are similar to the OLS results.[8] ”

However, Grossman uses city size, and not relative real wage growth, which was the Weber thesis, as his "main dependent variable" (Grossman, 2).

Other recent scholarship continues to find valid Protestant Ethic effects both in historical and contemporary development patterns.

Dudley and Blum write:

"Evidence of falling wages in Catholic cities and rising wages in Protestant cities between 1500 and 1750, during the spread of literacy in the vernacular, is inconsistent with most theoretical models of economic growth. In The Protestant Ethic, Weber suggested an alternative explanation based on culture. Here, a theoretical model confirms that a small change in the subjective cost of cooperating with strangers can generate a profound transformation in trading networks. In explaining urban growth in early-modern Europe, specifications compatible with human-capital versions of the neoclassical model and endogenous-growth theory are rejected in favor of a "small-world" formulation based on the Weber thesis."[9]

Revisionist criticism

H.M. Robertson, in his book Aspects of Economic Individualism, argued against the historical and religious claims of Weber. Robertson points out that capitalism began to flourish not in Britain, but in 14th century Italy, a decidedly different epoch. Since this is true, then the rise of capitalism cannot be attributed to Adam Smith, the Protestant Revolution, etc. In fact, Robertson goes further, and states that what happened in Britain was rather a retrogression from what was achieved in Italy centuries earlier.

Looking at the history of the development of economic thought, Robertson shows that Adam Smith and David Ricardo did not found economic science *de novo*. In fact, liberal economic theory was developed by French and Italian Catholics, who were influenced by the Scholastics. The British economic thought was rather a step backwards since it espoused the Labor Theory of Value, which had already been proved incorrect by the School of Salamanca.[10]

Other criticism

It has recently been suggested that Protestantism has indeed influenced positively the capitalist development of respective social systems not so much through the "Protestant ethics" but rather through the promotion of literacy.[11][12]

Becker and Wossmann at the University of Munich showed that literacy levels differing in religious areas can sufficiently explain the economic gaps cited by Weber. The results were supported even under a concentric diffusion model of Protestantism using distance from Wittenberg as a model.[13]

See also

- Iron cage
- Rationalization
- Disenchantment
- Protestant work ethic
- Social evolutionism
- Merton thesis
- Anglo-Saxon economy

References

1. ^ Max Weber; Peter R. Baehr; Gordon C. Wells (2002). *The Protestant ethic and the "spirit" of capitalism and other writings* (http://books.google.com/books?id=4MmligHndssC) . Penguin. ISBN 978-0-14-043921-2. http://books.google.com/books?id=4MmligHndssC. Retrieved 21 August 2011.

Max Weber, The Protestant Ethic and the Spirit of Capitalism. 1905

Read 10/24

Chapter II
The Spirit of Capitalism

In the title of this study is used the somewhat pretentious phrase, the spirit of capitalism. What is to be understood by it? The attempt to give anything like a definition of it brings out certain difficulties which are in the very nature of this type of investigation.

If any object can be found to which this term can be applied with any understandable meaning, it can only be an historical individual, i.e. a complex of elements associated in historical reality which we unite into a conceptual whole from the standpoint of their cultural significance.

Such an historical concept, however, since it refers in its content to a phenomenon significant for its unique individuality, cannot be defined according to the formula *genus proximunt, differentia specifica*, but it must be gradually put together out of the individual parts which are taken from historical reality to make it up. Thus the final and definitive concept cannot stand at the beginning of the investigation, but must come at the end. We must, in other words, work out in the course of the discussion, as its most important result, the best conceptual formulation of what we here understand by the spirit of capitalism, that is the best from the point of view which interests us here. This point of view (the one of which we shall speak later) is, further, by no means the only possible one from which the historical phenomena we are investigating can be analyzed. Other standpoints would, for this as for every historical phenomenon, yield other characteristics as the essential ones. The result is that it is by no means necessary to understand by the spirit of capitalism only what it will come to mean to us for the purposes of our analysis. This is a necessary result of the nature of historical concepts which attempt for their methodological purposes not to grasp historical reality in abstract general formulae, but in concrete genetic sets of relations which are inevitably of a specifically unique and individual character. too long...

Thus, if we try to determine the object, the analysis and historical explanation of which we are attempting, it cannot be in the form of a conceptual definition, but at least in the beginning only a provisional description of what is here meant by the spirit of capitalism. Such a description is, however, indispensable in order clearly to understand the object of the investigation. For this purpose we turn to a document of that spirit which contains what we are looking for in almost classical purity, and at the game time has the advantage of being free from all direct relationship to religion, being thus for our purposes, free of preconceptions.

Op cost

"Remember, that time is money. He that can earn ten shillings a day by his labor, and goes abroad, or sits idle, one half of that day, though he spends but sixpence during his diversion or idleness, ought not to reckon that the only expense; he has really spent, rather thrown away, five shillings, besides.

"Remember, that credit is money. If a man lets his money lie in my hands after it is due, he gives me interest, or so much as I can make of it during that time. This amounts to a considerable sum where a man has good and large credit, and makes good use of it.

Use now or Invest

"Remember, that money is of the prolific, generating nature. Money can beget money, and its offspring can beget more, and so on. Five shillings turned is six, turned again it is seven and three pence, and so on, till it becomes a hundred pounds. The more there is of it, the more it produces every turning, so that the profits rise quicker and quicker. He that kills a breeding sow, destroys all her offspring to the thousandth generation. He that murders a crown, destroys all that it might have produced, even scores of pounds."

"Remember this saying, *The good paymaster is lord of another man's purse* . He that is known to pay punctually and exactly to the time he promises, may at any time, and on any occasion, raise all the money his friends can spare. This is sometimes of great use. After industry and frugality, nothing contributes more to the raising of a young man in the world than punctuality and justice in all his dealings; therefore never keep borrowed money an hour beyond the time you promised, lest a disappointment shut up your friend's purse for ever.

"The most trifling actions that affect a man's credit are to be regarded. The sound of your hammer at five in the morning, or eight at night, heard by a creditor, makes him easy six months longer; but if he sees you at a billiard table, or hears your voice at a tavern, when you should be at work, he sends for his money the next day; demands it, before he can receive it, in a lump. 'It shows, besides, that you are mindful of what you owe; it makes you appear a careful as well as an honest man, and that still increases your credit.'

Credit is based on reputation

"Beware of thinking all your own that you possess, and of living accordingly. It is a mistake that many people who have credit fall into. To prevent this, keep an exact account for some time both of your expenses and your income. If you take the pains at first to mention particulars, it will have this good effect: you will discover how wonderfully small, trifling expenses mount up to large sums, and will discern what might have been, and may for the future be saved, without occasioning any great inconvenience.

Credit card statement :)

"For six pounds a year you may have the use of one hundred pounds, provided you are a man of known prudence and honesty.

"He that spends a groat a day idly, spends idly above six pounds a year, which is the price for the use of one hundred pounds.

"He that wastes idly a groat's worth of his time per day, one day with another, wastes the privilege of using one hundred pounds each day.

> "He that idly loses five shillings' worth of time, loses five shillings, and might as prudently throw five shillings into the sea.
>
> "He that loses five shillings, not only loses that sum, but all the advantage that might be made by turning it in dealing, which by the time that a young man becomes old, will amount to a considerable sum of money."

It is Benjamin Franklin who preaches to us in these sentences, the same which Ferdinand Kurnberger satirizes in his clever and malicious *Picture of American Culture* as the supposed confession of faith of the Yankee. That it is the spirit of capitalism which here speaks in characteristic fashion, no one will doubt, however little we may wish to claim that everything which could be understood as pertaining to that spirit is contained in it. Let us pause a moment to consider this passage, the philosophy of which Kurnberger sums up in the words, "They make tallow out of cattle and money out of men." The peculiarity of this philosophy of avarice appears to be the ideal of the honest man of recognized credit, and above all the idea of a duty of the individual toward the increase of his capital, which is assumed as an end in itself. Truly what is here preached is not simply a means of making one's way in the world, but a peculiar ethic. The infraction of its rules is treated not as foolishness but as forgetfulness of duty. That is the essence of the matter. It is not mere business astuteness, that sort of thing is common enough, it is an ethos. This is the quality which interests us.

lacking Courage

When Jacob Fugger, in speaking to a business associate who had retired and who wanted to persuade him to do the same, since he had made enough money and should let others have a chance, rejected that as pusillanimity and answered that "he (Fugger) thought otherwise, he wanted to make money as long as he could," the spirit of his statement is evidently quite different from that of Franklin. What in the former case was an expression of commercial daring and a personal inclination morally neutral, in the latter takes on the character of ethically colored maxim for the conduct of life. The concept spirit of capitalism is here used in this specific sense, it is the spirit of modern capitalism. For that we are here dealing only with Western European and American capitalism is obvious from the way in which the problem was stated. Capitalism existed in China, India, Babylon, in the classic world, and in the Middle Ages. But in all these cases, as we shall see, this particular ethos was lacking. how do we know that?

Now, all Franklin's moral attitudes are colored with utilitarianism. Honesty is useful, because it assures credit; so are punctuality, industry, frugality, and that is the reason they are virtues. A logical deduction from this would be that where, for instance, the appearance of honesty serves the same purpose, that would suffice, and an unnecessary surplus of this virtue would evidently appear to Franklin's eyes a unproductive waste. And as a matter of fact, the story in his autobiography of his conversion to those virtues, or the

I think I am most like Ben Franklin

discussion of the value of a strict maintenance of the appearance of modesty, the assiduous belittlement of one's own deserts in order to gain general recognition later, confirms this impression. According to Franklin, those virtues, like all others, are only in so far virtues as they are actually useful to the individual, and the surrogate of mere appearance is always sufficient when it accomplishes the end in view. It is a conclusion which is inevitable for strict utilitarianism. The impression of many Germans that the virtues professed by Americanism are pure hypocrisy seems to have been confirmed by this striking case. But in fact the matter is not by any means so simple.

Benjamin Franklin's own character, as it appears in the really unusual candidness of his autobiography, belies that suspicion. The circumstance that he ascribes his recognition of the utility of virtue to a divine revelation which was intended to lead him in the path of righteousness, shows that something more than mere garnishing for purely egocentric motives is involved.

In fact, the *summum bonum* of his ethic, the earning of more and more money, combined with the strict avoidance of all spontaneous enjoyment of life, is above all completely devoid of any eudaemonistic, not to say hedonistic, admixture. It is thought of so purely as an end in itself, that from the point of view of the happiness of, or utility to, the single individual, it appears entirely transcendental and absolutely irrational. Man is dominated by the making of money, by acquisition as the ultimate purpose of his life. Economic acquisition is no longer subordinated to man as the means for the satisfaction of his material needs. This reversal of what we should call the natural relationship, so irrational from a naive point of view, is evidently as definitely a leading principle of capitalism as it is foreign to all peoples not under capitalistic influence. At the same time it expresses a type of feeling which is closely connected with certain religious ideas. If we thus ask, *why* should "money be made out of men," Benjamin Franklin himself, although he was a colorless deist, answers in his autobiography with a quotation from the Bible, which his strict Calvinistic father drummed into him again and again in his youth: "Seest thou a man diligent in his business? He shall stand before kings" (Prov. xxii. 29). The earning of money within the modern economic order is, so long as it is done legally, the result and the expression of virtue and proficiency in a calling; and this virtue and proficiency are, as it is now not difficult to see, the real Alpha and Omega of Franklin's ethic, as expressed in the passages we have quoted, as well as in all his works without exception.

hard work, not pleasure

And in truth this peculiar idea, so familiar to us today, but in reality so little a matter of course, of one's duty in a calling, is what is most characteristic of the social ethic of capitalistic culture, and is in a sense the fundamental basis of it. It is an obligation which the individual is supposed to feel and does feel towards the content of his professional activity, no matter in what it consists, in particular no matter whether it appears on the surface as a utilization of his personal powers, or only of his material possessions (as capital).

Of course, this conception has not appeared only under capitalistic conditions. On the contrary, we shall later trace its origins back to a time previous to the advent of capitalism. Still less, naturally, do we maintain: that a conscious acceptance of these ethical maxims on the part of the individuals, entrepreneurs or laborers in modern capitalistic enterprises, is a condition of the further existence of present day capitalism. The capitalistic economy of the present day is an immense cosmos into which the individual is born, and which presents itself to him, at least as an individual, as an unalterable order of things in which he must live. It forces the individual, in so far as he is involved in the system of market relationships, to conform to capitalistic rules of action. The manufacturer who in the long run acts counter to these norms, will just as inevitably be eliminated from the economic scene as the worker who cannot or will not adapt himself to them will be thrown into the streets without a job.

Thus the capitalism of today, which has come to dominate economic life, educates and selects the economic subjects which it needs through a process of economic survival of the fittest. But here one can easily see the limits of the concept of selection as a means of historical explanation. In order that a manner of life so well adapted to the peculiarities of capitalism could be selected at all, i.e. should come to dominate others, it had to originate somewhere, and not in isolated individuals alone, but as a way of life common to whole groups of men. This origin is what really needs explanation. Concerning the doctrine of the more naive historical materialism, that such ideas originate as a reflection or superstructure of economic situations, we shall speak more in detail below. At this point it will suffice for our purpose to call attention to the fact that without doubt, in the country of Benjamin Franklin's birth (Massachusetts), the spirit of capitalism (in the sense we have attached to it) was present before the capitalistic order. There were complaints of a peculiarly calculating sort of profit-seeking in New England, as distinguished from other parts of America, as early as 1632. It is further undoubted that capitalism remained far less developed in some of the neighboring colonies, the later Southern States of the United States of America, in spite of the fact that these latter were founded by large capitalists for business motives, while the New England colonies were founded by preachers and seminary graduates with the help of small bourgeois, craftsmen and yoemen, for religious reasons. In this case the causal relation is certainly the reverse of that suggested by the materialistic standpoint.

work the ethic has led to material wealth

But the origin and history of such ideas is much more complex than the theorists of the superstructure suppose. The spirit of capitalism, in the sense in which we are using the term, had to fight its way to supremacy against a whole world of hostile forces. A state of mind such as that expressed in the passages we have quoted from Franklin, and which called forth the applause of a whole people, would both in ancient times and in the Middle Ages have been proscribed as the lowest sort of avarice and as an attitude entirely lacking in self-respect. It is, in fact, still regularly thus looked upon by all those social groups which are least involved in or adapted to modern capitalistic conditions. This is not wholly because the instinct of acquisition was in those times unknown or undeveloped, as has often been said. Nor because the *auri sacra fames*, the greed for gold, was then, or now, less powerful outside of bourgeois capitalism than within its peculiar sphere, as the illusions of modern romanticists are wont to believe. The difference between the capitalistic and pre-capitalistic spirits is not to be found at this point. The greed of the Chinese Mandarin, the old Roman aristocrat, or the modern peasant, can stand up to any comparison. And the *auri sacra fames* of a Neapolitan cab-driver or *barcaiuolo*, and certainly of Asiatic representatives of similar trades, as well as of the craftsmen of southern European or Asiatic countries is, as anyone can find out for himself, very much more intense, and especially more unscrupulous than that of, say, an Englishman in similar circumstances.

The universal reign of absolute unscrupulousness in the pursuit of selfish interests by the making of money has been a specific characteristic of precisely those countries whose bourgeois-capitalistic development, measured according to Occidental standards, has remained backward. As every employer knows, the lack of *coscienziosita* of the labourers of such countries, for instance Italy as compared with Germany, has been, and to a certain extent still is, one of the principal obstacles to their capitalistic development. Capitalism cannot make use of the labor of those who practice the doctrine of undisciplined *liberum arbitrium*, any more than it can make use of the business man who seems absolutely unscrupulous in his dealings with others, as we can learn from Franklin. Hence the difference does not lie in the degree of development of any impulse to make money. The *auri sacra fames* is as old as the history of man. But we shall see that those who submitted to it without reserve as an uncontrolled impulse, such as the Dutch sea captain who "would go through hell for gain, even though he scorched his sails," were by no means the representatives of that attitude of mind from which the specifically modern capitalistic spirit as a mass phenomenon is derived, and that is what matters. At all periods of history, wherever it was possible, there has been ruthless acquisition, bound to, no ethical norms whatever. Like war and piracy, trade has often been unrestrained in its relations with foreigners and those outside the group. The double ethic has permitted here what was forbidden in dealings among brothers.

free will

hard work

Capitalistic acquisition as an adventure has been at home in all types of economic society which have known trade with the use of money and which have offered it opportunities, through *commenda*, farming of taxes, State loans, financing of wars, ducal courts and office-holders. Likewise the inner attitude of the adventurer, which laughs at all ethical limitations, has been universal. Absolute and conscious ruthlessness in acquisition has often stood in the closest connection with the strictest conformity to tradition. Moreover, with the breakdown of tradition and the more or less complete extension of free economic enterprise, even to within the social group, the new thing has not generally been ethically justified and encouraged, but only tolerated as a fact. And this fact has been treated either as ethically indifferent or as reprehensible, but unfortunately unavoidable. This has not only been the normal attitude of all ethical teachings, but, what is more important, also that expressed in the practical action of the average man of pre-capitalistic times, pre-capitalistic in the sense that the rational utilization of capital in a permanent enterprise and the rational capitalistic organization of labor had not yet become dominant forces in the determination of economic activity. Now just this attitude was one of the strongest inner obstacles which the adaptation of men to the conditions of an ordered bourgeois-capitalistic economy has encountered everywhere.

The most important opponent with which the spirit of capitalism, in the sense of a definite standard of life claiming ethical sanction, has had to struggle, was that type of attitude and reaction to new situations which we may designate as traditionalism. In this case also every attempt at a final definition must be held in abeyance. On the other hand, we must try to make the provisional meaning clear by citing a few cases. We will begin from below, with the laborers.

One of the technical means which the modern employer uses in order to secure the greatest possible amount of work from his men is the device of piece rates. In agriculture, for instance, the gathering of the harvest is a case where the greatest possible intensity of labor is called for, since, the weather being uncertain, the difference between high profit and heavy loss may depend on the speed with which the harvesting can be done. Hence a system of piece rates is almost universal in this case. And since the interest of the employer in a speeding up of harvesting increases with the increase of the results and the intensity of the work, the attempt has again and again been made, by increasing the piece rates of the workmen, thereby giving them an opportunity to earn what is for them a very high wage, to interest them in increasing their own efficiency. But a peculiar difficulty has been met with surprising frequency: raising the piece rates has often had the result that not more but less has been accomplished in the same time, because the worker reacted to the increase not by increasing but by decreasing the amount of his work. A man, for instance, who at the rate of 1 mark per acre mowed 2½ acres per day and earned 2½ marks, when the rate was raised to 1¼ marks per acre mowed, not 3 acres, as be might easily have done, thus earning 3¾ marks, but only 2 acres, so that he could still earn the 2½ marks to which he was accustomed. The opportunity of earning more was less attractive than that of working less. He did not ask: how much can I earn in a day if I do as much work as possible? but: how much must I work in order to earn the wage, 2½ marks, which I earned before and which takes care of my traditional needs? This is an example of what is here meant by traditionalism. A man does not "by nature" wish to cam more and more money, but simply to live as he is accustomed to live and to earn as much as is necessary for that purpose. Wherever modern capitalism has begun its work of increasing the productivity of human labor by increasing its intensity, it has encountered the immensely stubborn resistance of this leading trait of pre-capitalistic labor. And today it encounters it the more, the more backward (from a capitalistic point of view) the laboring forces are with which it has to deal.

very much depends on person

Another obvious possibility, to return to our example, since the appeal to the acquisitive instinct through higher wage rates failed, would have been to try the opposite policy, to force the worker by reduction of his wage rates to work harder to cam the same amount than he did before. Low wages and high profits seem even today to a superficial observer to stand in correlation; everything which is paid out in wages seems to involve a corresponding reduction of profits. That road capitalism has taken again and again since its beginning. For centuries it was an article of faith, that low wages were productive, i.e. that they increased the material results of labor so that, as Pieter de la Cour, on this point, as we shall see, quite in the spirit of the old Calvinism, said long ago, the people only work because and so long as they are poor.

61 - how do you even attempt to prove that!

But the effectiveness of this apparently so efficient method has its limits. Of course the presence of a surplus population which it can hire cheaply in the labour market is a necessity for the development of capitalism. But though too large a reserve army may in certain cases favor its quantitative expansion, it checks its qualitative development, especially the transition to types of enterprise which make more intensive use of labor. Low wages are by no means identical with cheap labor. From a purely quantitative point of view the efficiency of labor decreases with a wage which is physiologically insufficient, which may in the long run even mean a survival of the unfit. The present-day average Silesian mows, when he exerts himself to the full, little more than two thirds as much land as the better paid and nourished Pomeranian or Mecklenburger, and the Pole, the further East he comes from, accomplishes progressively less than the German. Low wages fail even from a purely business point of view wherever it is a question of producing goods which require any sort of skilled labor, or the use of expensive machinery which is easily damaged, or in general wherever any great amount of sharp attention or of initiative is required. Here low wages do not pay, and their effect is the opposite of what was intended. For not only is a developed sense of responsibility absolutely indispensable, but in general also an attitude which, at least during working hours, is freed from continual calculations of how the customary wage may be earned with a maximum of comfort and a minimum of exertion. Labor must, on the contrary, be performed as if it were an absolute end in itself, a calling. But such an attitude is by no means a product of nature. It cannot be evoked by low wages or high ones alone, but can only be the product of a long and arduous process of education. Today, capitalism, once in the saddle, can recruit its laboring force in all industrial countries with comparative ease. In the past this was in every case an extremely difficult problem. And even today it could probably not get along without the support of a powerful ally along the way, which, as we shall see below, was at hand at the time of its development.

What is meant can again best be explained by means of an example. The type of backward traditional form of labor is today very often exemplified by women workers, especially unmarried ones. An almost universal complaint of employers of girls, for instance German girls, is that they are almost entirely unable and unwilling to give up methods of work inherited or once learned in favor of more efficient ones, to adapt themselves to new methods, to learn and to concentrate their intelligence, or even to use it at all. Explanations of the possibility of making work easier, above all more profitable to themselves, generally encounter a complete lack of understanding. Increases of piece rates are without avail against the stone wall of habit. In general it is otherwise, and that is a point of no little importance from our viewpoint, only with girls having a specifically religious, especially a Pietistic, background. One often hears, and statistical investigation confirms it, that by far the best chances of economic education are found among this group. The ability of mental concentration, as well as the absolutely essential feeling of obligation to one's job, are here most often combined with a strict economy which calculates the possibility of high earnings, and a cool self-control and frugality which enormously increase performance. This provides the most favorable foundation for the conception of labor as an end in itself, as a calling which is necessary to capitalism: the chances of overcoming traditionalism are greatest on account of the religious upbringing. This observation of present-day capitalism in itself suggests that it is worth while to ask how this connection of adaptability to capitalism with religious factors may have come about in the days of the early development of capitalism. For that they were even then present in much the same form can be inferred from numerous facts. For instance, the dislike and the persecution which Methodist workmen in the eighteenth century met at the hands of their comrades were not solely nor even principally the result of their religious eccentricities, England had seen many of those and more striking ones. It rested rather, as the destruction of their tools, repeatedly mentioned in the reports, suggests, upon their

wait religion helps or hurts?

specific willingness to work as we should say today.

However, let us again return to the present, and this time to the entrepreneur, in order to clarify the meaning of traditionalism in his case. Sombart, in his discussions of the genesis of capitalism, has distinguished between the satisfaction of needs and acquisition as the two great leading principles in economic history. In the former case the attainment of the goods necessary to meet personal needs, in the latter a struggle for profit free from the limits set by needs, have been the ends controlling the form and direction of economic activity. What he called the economy of needs seems at first glance to be identical with what is here described as economic traditionalism. That may be the case if the concept of needs is limited to traditional needs. But if that is not done, a number of economic types which must be considered capitalistic according to the definition of capital which Sombart gives in another part of his work, would be excluded from the category of acquisitive economy and put into that of needs economy. Enterprises, namely, which are carried on by private entrepreneurs by utilizing capital (money or goods with a money value) to make a profit, purchasing the means of production and selling the product, i.e. undoubted capitalistic enterprises, may at the same time have a traditionalistic character. This has, in the course even of modern economic history, not been merely an occasional case, but rather the rule, with continual interruptions from repeated and increasingly powerful conquests of the capitalistic spirit. To be sure the capitalistic form of an enterprise and the spirit in which it is run generally stand in some sort of adequate relationship to each other, but not in one of necessary interdependence. Nevertheless, we provisionally use the expression spirit of (modern) capitalism to describe that attitude which seeks profit rationally and systematically in the manner which we have illustrated, by the example of Benjamin Franklin. This, however, is justified by the historical fact that that attitude of mind has on the one hand found its most suitable expression in capitalistic enterprise, while on the other the enterprise has derived its most suitable motive force from the spirit of capitalism.

But the two may very well occur separately. Benjamin Franklin was filled with the spirit of capitalism at a time when his printing business did not differ in form from any handicraft enterprise. And we shall see that at the beginning of modern times it was by no means the capitalistic entrepreneurs of the commercial aristocracy, who were either the sole or the predominant bearers of the attitude we have here called the spirit of capitalism. It was much more the rising strata of the lower industrial middle classes. Even in the nineteenth century its classical representatives were not the elegant gentlemen of Liverpool and Hamburg, with their commercial fortunes handed down for generations, but the self-made parvenus of Manchester and Westphalia, who often rose from very modest circumstances. As early as the sixteenth century the situation was similar; the industries which arose at that time were mostly created by parvenus.

The management, for instance, of a bank, a wholesale export business, a large retail establishment, or of a large putting-out enterprise dealing with goods produced in homes, is certainly only possible in the form of a capitalistic enterprise. Nevertheless, they may all be carried on in a traditionalistic spirit. In fact, the business of a large bank of issue cannot be carried on in any other way. The foreign trade of whole epochs has rested on the basis of monopolies and legal privileges of strictly traditional character. In retail trade – and we are not here talking of the small men without capital who are continually crying out for Government aid – the revolution which is making an end of the old traditionalism is still in full swing. It is the same development which broke up the old putting-out system, to which modern domestic labor is related only in form. How this revolution takes place and what is its significance may, in spite of the fact these things are so familiar, be again brought out by a concrete example.

Until about the middle of the past century the life of a putter-out was, at least in many of the branches of the Continental textile industry, what we should today consider very comfortable. We may imagine its routine somewhat as follows: The peasants came with their cloth, often (in the case of linen) principally or entirely made from raw material which the peasant himself had produced, to the town in which the putter-out lived, and after a careful, often official, appraisal of the quality, received the customary price for it. The putter-out's customers, for markets any appreciable distance away, were middlemen, who also came to him, generally not yet following samples, but seeking traditional qualities, and bought from his warehouse, or, long before delivery, placed orders which were probably in turn passed on to the peasants. Personal canvassing of customers took place, if at all, only at long intervals. Otherwise correspondence sufficed, though the sending of samples slowly gained ground. The number of business hours was very moderate, perhaps five to six a day, sometimes considerably less; in the rush season, where there was one, more. Earnings were moderate; enough to lead a respectable life and in good times to put away a little. On the whole, relations among competitors were relatively good, with a large degree of agreement on the fundamentals of business. A long daily visit to the tavern, with often plenty to drink, and a congenial circle of friends, made life comfortable and leisurely.

Sloth

The form of organization was in every respect capitalistic; the entrepreneur's activity was of a purely business character; the use of capital, turned over in the business, was indispensable; and finally, the objective aspect of the economic process, the book-keeping, was rational. But it was traditionalistic business, if one considers the spirit which animated the entrepreneur: the traditional manner of life, the traditional rate of profit, the traditional amount of work, the traditional manner of regulating the relationships with labor, and the essentially traditional circle of customers and the manner of attracting new ones. All these dominated the conduct of the business, were at the basis, one may say, of the ethos of this group of business men.

Traditional

Now at some time this leisureliness was suddenly destroyed, and often entirely without any essential change in the form of organization, such as the transition to a unified factory, to mechanical weaving, etc. What happened was, on the contrary, often no more than this: some young man from one of the putting-out families went out into the country, carefully chose weavers for his employ, greatly increased the rigor of his supervision of their work, and thus turned them from peasants into laborers. On the other hand, he would begin to change his marketing methods by so far as possible going directly to the final consumer, would take the details into his own hands, would personally solicit customers, visiting them every year, and above all would adapt the quality of the product directly to their needs and wishes. At the same time he began to introduce the principle of low prices and large turnover. There was repeated what everywhere and always is the result of such a process of rationalization: those who would not follow suit had to go out of business. The idyllic state collapsed under the pressure of a bitter competitive struggle, respectable fortunes were made, and not lent out at interest, but always reinvested in the business. The old leisurely and comfortable attitude toward life gave way to a hard frugality in which some participated and came to the top, because they did not wish to consume but to earn, while others who wished to keep on with the old ways were forced to curtail their consumption.

I don't know if the old System was all that idellic

And, what is most important in this connection, it was not generally in such cases a stream of new money invested in the industry which brought about this revolution – in several cases known to me the whole revolutionary process was set in motion with a few thousands of capital borrowed from relations – but the new spirit, the spirit of modern capitalism, had set to work. The question of the motive forces in the expansion of modern capitalism is not in the first instance a question of the origin of the capital sums which were available for capitalistic uses, but, above all, of the development of the spirit of capitalism. Where it appears and is able to work itself out, it produces its own capital and monetary supplies as the means to its ends, but the reverse is not true. Its entry on the scene was not generally peaceful. A flood of mistrust, sometimes of hatred, above all of moral indignation, regularly opposed itself to the first innovator. Often – I know of several cases of the sort – regular legends of mysterious shady spots in his previous life have been produced. It is very easy not to recognize that only an unusually strong character could save an entrepreneur of this new type from the loss of his temperate self-control and from both moral and economic shipwreck. Furthermore, along with clarity of vision and ability to act, it is only by virtue of very definite and highly developed ethical qualities that it has been possible for him to command the absolutely indispensable confidence of his customers and workmen. Nothing else could have given him the strength to overcome the innumerable obstacles, above all the infinitely more intensive work which is demanded of the modern entrepreneur. But these are ethical qualities of quite a different sort from those adapted to the traditionalism of the past.

And, as a rule, it has been neither dare-devil and unscrupulous speculators, economic adventurers such as we meet at all periods of economic history, nor simply great financiers who have carried through this change, outwardly so inconspicuous, but nevertheless so decisive for the penetration of economic life with the new spirit. On the contrary, they were men who had grown up in the hard school of life, calculating and daring at the same time, above all temperate and reliable, shrewd and completely devoted to their business, with strictly bourgeois opinions and principles. One is tempted to think that these personal moral qualities have not the slightest relation to any ethical maxims, to say nothing of religious ideas, but that the essential relation between them is negative. The ability to free oneself from the common tradition, a sort of liberal enlightenment, seems likely to be the most suitable basis for such a business man's success. And today that is generally precisely the case. Any relationship between religious beliefs and conduct is generally absent, and where any exists, at least in Germany, it tends to be of the negative sort. The people filled with the spirit of capitalism today tend to be indifferent, if not hostile, to the Church. The thought of the pious boredom of paradise has little attraction for their active natures; religion appears to them as a means of drawing people away from labor in this world. If you ask them what is the meaning of their restless activity, why they are never satisfied with what they have, thus appearing so senseless to any purely worldly view of life, they would perhaps give the answer, if they know any at all: "to provide for my children and grandchildren." But more often and, since that motive is not peculiar to them, but was just as effective for the traditionalist, more correctly, simply: that business with its continuous work has become a necessary part of their lives. That is in fact the only possible motivation, but it at the same time expresses what is, seen from the viewpoint of personal happiness, so irrational about this sort of life, where a man exists for the sake of his business, instead of the reverse.

from the title this seemed so much better!

free from tradition / innovative

I don't tie the 2 together

Of course, the desire for the power and recognition which the mere fact of wealth brings plays its part. When the imagination of a whole people has once been turned toward purely quantitative bigness, as in the United States, this romanticism of numbers exercises an irresistible appeal to the poets among business men. Otherwise it is in general not the real leaders, and especially not the permanently successful entrepreneurs, who are taken in by it. In particular, the resort to entailed estates and the nobility, with sons whose conduct at the university and in the officers' corps tries to cover up their social origin, as has been the typical history of German capitalistic parvenu families, is a product of later decadence. The ideal type of the capitalistic entrepreneur, as it has been represented even in Germany by occasional outstanding examples, has no relation to such more or less refined climbers. He avoids ostentation and unnecessary expenditure, as well as conscious enjoyment of his power, and is embarrassed by the outward signs of the social recognition which he receives. His manner of life is, in other words, often, and we shall have to investigate the historical significance of just this important fact, distinguished by a certain ascetic tendency, as appears clearly enough in the sermon of Franklin which we have quoted. It is, namely, by no means exceptional, but rather the rule, for him to have a sort of modesty which is essentially more honest than the reserve which Franklin so shrewdly recommends. He gets nothing out of his wealth for himself, except the irrational sense of having done his job well.

But it is just that which seems to the pre-capitalistic man so incomprehensible and mysterious, so unworthy and contemptible. That anyone should be able to make it the sole purpose of his life-work, to sink into the grave weighed down with a great material load of money and goods, seems to him explicable only as the product of a perverse instinct, the *auri sacra fames*. greed for gold — Why would anyone work for work's sake?

At present under our individualistic political, legal, and economic institutions, with the forms of organization and general structure which are peculiar to our economic order, this spirit of capitalism might be understandable, as has been said, purely as a result of adaptation. The capitalistic system so needs this devotion to the calling of making money, it is an attitude toward material goods which is so well suited to that system, so intimately bound up with the conditions of survival in the economic struggle for existence, that there can today no longer be any question of a necessary connection of that acquisitive manner of life with any single *Weltanschauung* . In fact, it no longer needs the support of any religious forces, and feels the attempts of religion to influence economic life, in so far as they can still be felt at all, to be as much an unjustified interference as its regulation by the State. In such circumstances men's commercial and social interests do tend to determine their opinions and attitudes. Whoever does not adapt his manner of life to the conditions of capitalistic success must go under, or at least cannot rise. But these are phenomena of a time in which modern capitalism has become dominant and has become emancipated from its old supports. But as it could at one time destroy the old forms of medieval regulation of economic life only in alliance with the growing power of the modern State, the same, we may say provisionally, may have been the case in its relations with religious forces. Whether and in what sense that was the case, it is our task to investigate. For that the conception of money-making as an end in itself to which people were bound, as a calling,

religion → god
-tradition + hard work

was contrary to the ethical feelings of whole epochs, it is hardly necessary to prove. The dogma *Deo placere vix potest* which was incorporated into the canon law and applied to the activities of the merchant, and which at that time (like the passage in the gospel about interest) was considered genuine, as well as St. Thomas's characterization of the desire for gain as *turpitudo* (which term even included unavoidable and hence ethically justified profit making), already contained a high degree of concession on the part of the Catholic doctrine to the financial powers with which the Church had such intimate political relations in the Italian cities, as compared with the much more radically anti-chrematistic views of comparatively wide circles. But even where the doctrine was still better accommodated to the facts, as for instance with Anthony of Florence, the feeling was never quite overcome, that activity directed to acquisition for its own sake was at bottom a *pudendum* which was to be tolerated only because of the unalterable necessities of life in this world.

Some moralists of that time, especially of the nominalistic school, accepted developed capitalistic business forms as inevitable, and attempted to justify them, especially commerce, as necessary. The *industria* developed in it they were able to regard, though not without contradictions, as a legitimate source of profit, and hence ethically unobjectionable. But the dominant doctrine rejected the spirit of capitalistic acquisition as *turpitudo*, or at least could not give it a positive ethical sanction. An ethical attitude like that of Benjamin Franklin would have been simply unthinkable. This was, above all, the attitude of capitalistic circles themselves. Their life-work was, so long as they clung to the tradition of the Church, at best something morally indifferent. It was tolerated, but was still, even if only on account of the continual danger of collision with the Church's doctrine on usury, somewhat dangerous to salvation. Quite considerable sums, as the sources show, went at the death of rich people to religious institutions as conscience money, at times even back to former debtors as *usura* which had been unjustly taken from them. It was otherwise, along with heretical and other tendencies looked upon with disapproval, only in those parts of the commercial aristocracy which were already emancipated from the tradition. But even skeptics and people indifferent to the Church often reconciled themselves with it by gifts, because it was a sort of insurance against the uncertainties of what might come after death, or because (at least according to the very widely held latter view) an external obedience to the commands of the Church was sufficient to insure salvation. Here the either non-moral or immoral character of their action in the opinion of the participants themselves comes clearly to light.

Now, how could activity, which was at best ethically tolerated, turn into a calling in the sense of Benjamin Franklin? The fact to be explained historically is that in the most highly capitalistic center of that time, in Florence of the fourteenth and fifteenth centuries, the money and capital market of all the great political powers, this attitude was considered ethically unjustifiable, or at best to be tolerated. But in the backwoods small bourgeois circumstances of Pennsylvania in the eighteenth century, where business threatened for simple lack of money to fall back into barter, where there was hardly a sign of large enterprise, where only the earliest beginnings of banking were to be found, the same thing was considered the essence of moral conduct, even commanded in the name of duty. To speak here of a reflection of material conditions in the ideal superstructure would be patent nonsense. What was the background of ideas which could account for the sort of activity apparently directed toward profit alone as a calling toward which the individual feels himself to have an ethical obligation? For it was this idea which gave the way of life of the new entrepreneur its ethical foundation and justification.

The attempt has been made, particularly by Sombart, in what are often judicious and effective observations, to depict economic rationalism as the salient feature of modern economic life as a whole. Undoubtedly with justification, if by that is meant the extension of the productivity of labor which has, through the subordination of the process of production to scientific points of view, relieved it from its dependence upon the natural organic limitations of the human individual. Now this process of rationalization in the field of technique and economic organization undoubtedly determines an important part of the ideals of life of modern bourgeois society. Labor in the service of a rational organization for the provision of humanity with material goods has without doubt always appeared to representatives of the capitalistic spirit as one of the most important purposes of their life-work. It is only necessary, for instance, to read Franklin's account of his efforts in the service of civic improvements in Philadelphia clearly to apprehend this obvious truth. And the joy and pride of having given employment to numerous people, of having had a part in the economic progress of his home town in the sense referring to figures of population and volume of trade which capitalism associated with the word, all these things obviously are part of the specific and undoubtedly idealistic satisfactions in life to modern men of business. Similarly it is one of the fundamental characteristics of an individualistic capitalistic economy that it is rationalized on the basis of rigorous calculation, directed with foresight and caution toward the economic success which is sought in sharp contrast to the hand-to-mouth existence of the peasant, and to the privileged traditionalism of the guild craftsman and of the adventurers' capitalism, oriented to the exploitation of political opportunities and irrational speculation.

think I'm like Franklin

Capitalism more for astetic appeal

It might thus seem that the development of the spirit of capitalism is best understood as part of the development of rationalism as a whole, and could be deduced from the fundamental position of rationalism on the basic problems of life. In the process Protestantism would only have to be considered in so far as it had formed a stage prior to the development of a purely rationalistic philosophy. But any serious attempt to carry this thesis through makes it evident that such a simple way of putting the question will not work, simply because of the fact that the history of rationalism shows a development which by no means follows parallel lines in the various departments of life. The rationalization of private law, for instance, if it is thought of as a logical simplification and rearrangement of the content of the law, was achieved in the highest hitherto known degree in the Roman law of late antiquity. But it remained most backward in some of the countries with the highest degree of economic rationalization, notably in England, where the Renaissance of Roman Law was overcome by the power of the great legal corporations, while it has always retained its supremacy in the Catholic countries of Southern Europe. The worldly rational philosophy of the eighteenth century did not find favor alone or even principally in the countries of highest capitalistic development. The doctrines of Voltaire are even today the common property of broad upper, and what is practically more important, middle class groups in the Romance Catholic countries. Finally, if under practical rationalism is understood the type of attitude which sees and judges the world consciously in terms of the worldly interests of the individual ego, then this view of life was and is the special peculiarity of the peoples of the *liberum arbitrium*, such as the Italians and the French are in very flesh and blood. But we have already convinced ourselves that this is by no means the soil in which that relationship of a man to his calling as a task, which is necessary to capitalism, has pre-eminently grown. In fact, one may – this simple proposition, which is often forgotten, should be placed at the beginning of every study which essays to deal with rationalism – rationalize life from fundamentally different basic points of view and in very different directions. Rationalism is an historical concept which covers a whole world of different things. It will be our task to find out whose intellectual child the particular concrete form of rational thought was, from which the idea of a calling and the devotion to labor in the calling has grown, which is, as we have seen, so irrational from the standpoint of purely eudaemonistic self-interest, but which has been and still is one of the most characteristic elements of our capitalistic culture. We are here particularly interested in the origin of precisely the irrational element which lies in this, as in every conception of a calling.

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Chapter V
Asceticism and the Spirit of Capitalism

In order to understand the connection between the fundamental religious ideas of ascetic Protestantism and its maxims for everyday economic conduct, it is necessary to examine with especial care such writings as have evidently been derived from ministerial practice. For in a time in which the beyond meant everything, when the social position of the Christian depended upon his admission to the communion, the clergyman, through his ministry, Church discipline, and preaching, exercised an influence (as a glance at collections of *consilia, casus conscientia*, etc., shows) which we modern men are entirely unable to picture. In such a time the religious forces which express themselves through such channels are the decisive influences in the formation of national character.

For the purposes of this chapter, though by no means for all purposes, we can treat ascetic Protestantism as a single whole. But since that side of English Puritanism which was derived from Calvinism gives the most consistent religious basis for the idea of the calling, we shall, following our previous method, place one of its representatives at the centre of the discussion. Richard Baxter stands out above many other writers on Puritan ethics, both because of his eminently practical and realistic attitude, and, at the same time, because of the universal recognition accorded to his works, which have gone through many new editions and translations. He was a Presbyterian and an apologist of the Westminster Synod, but at the same time, like so many of the best spirits of his time, gradually grew away from the dogmas of pure Calvinism. At heart he opposed Cromwell's usurpation as he would any revolution. He was unfavourable to the sects and the fanatical enthusiasm of the saints, but was very broad-minded about external peculiarities and objective towards his opponents. He sought his field of labour most especially in the practical promotion of the moral life through the Church. In the pursuit of this end, as one of the most successful ministers known to history, he placed his services at the disposal of the Parliamentary Government, of Cromwell, and of the Restoration until he retired from office under the last, before St. Bartholomew's day. His Christian Directory is the most complete compendium of Puritan ethics, and is adjusted to the practical experiences of his own ministerial activity. In comparison we shall see, Spener's *Theologische Bedenken*, as representative of German Pietism, Barclay's *Apology for the Quakers* and some other representatives of ascetic ethics, which, however, in the interest of space, will be limited as far as possible.

Now, in glancing at Baxter's *Saints' Everlasting Rest*, or his *Christian Directory*, or similar works of others, one is struck at first glance by the emphasis placed, in the discussion of wealth and its acquisition, on the ebionitic elements of the New testament. Wealth as such is a great danger; its temptations never end and its pursuit is not only senseless as compared with the dominating importance of the Kingdom of God, but it is morally suspect. Here asceticism seems to have turned much more sharply against the acquisition of earthly goods than it did in Calvin, who saw no hindrance to the effectiveness of the clergy in their wealth, but rather a thoroughly desirable enhancement of their prestige. Hence he permitted them to employ their means profitably. Examples of the condemnation of the pursuit of money and goods may be gathered without end from Puritan writings, and may be contrasted with the late mediaeval ethical literature, which was much more open-minded on this point. Moreover, these doubts were meant with perfect seriousness; only it is necessary to examine them somewhat more closely in order to understand their true ethical significance and implications. The real, moral objection is to relaxation in the security of possession, the enjoyment of wealth with the consequence of idleness and the temptations of the flesh, above all of distraction from the pursuit of a righteous life. In fact, it is only because possession involves this danger of relaxation that it is objectionable at all. For the saints' everlasting rest is in the next world; on earth man must, to be certain of his state of grace, "do the works of Him who sent him, as long as it is yet day." Not leisure and enjoyment, but only activity serves to increase the glory of God, according to the definite manifestations of His will.

Waste of time is thus the first and in principle the deadliest of sins. The span of human life is infinitely short and precious to make sure of one's own election. Loss of time through sociability, idle talk, luxury, even more sleep than is necessary for health, six to at most eight hours, is worthy of absolute moral condemnation. It does not yet hold, with Franklin, that time is money, but the proposition is true in a certain spiritual sense. It is infinitely valuable because every hour lost is lost to labour for the glory of God. Thus inactive contemplation is also valueless, or even directly reprehensible if it is at the expense of one's daily work. For it is less pleasing to God than the active performance of His will in a calling. Besides, Sunday is provided for that, and, according to Baxter, it is always those who are not diligent in their callings who have no time for God when the occasion demands it. *

Accordingly, Baxter's principal work is dominated by the continually repeated, often almost passionate preaching of hard, continuous bodily or mental labour. It is due to a combination of two different motives. Labour is, on the one hand, an approved ascetic technique, as it always has been in the Western Church, in sharp contrast not only to the Orient but to almost all monastic rules the world over. It is in particular the specific

Keeps people busy + prepare benefit

defence against all those temptations which Puritanism united under the name of the unclean life, whose role for it was by no means small. The sexual asceticism of Puritanism differs only in degree, not in fundamental principle, from that of monasticism; and on account of the Puritan conception of marriage, its practical influence is more far-reaching than that of the latter. For sexual intercourse is permitted, even within marriage, only as the means willed by God for the increase of His glory according to the commandment, "Be fruitful and Multiply." Along with a moderate vegetable diet and cold baths, the same prescription is given for all sexual temptations as is used against religious doubts and a sense of moral unworthiness: "Work hard in your calling." But the most important thing was that even beyond that labour came to be considered in itself the end of life, ordained as such by God. St. Paul's "He who will not work shall not eat" holds unconditionally for everyone. Unwillingness to work is symptomatic of the lack of grace.

Here the difference from the medieval viewpoint becomes quite evident. Thomas Aquinas also gave an interpretation of that statement of St. Paul. But for him labour is only necessary *naturali ratione* for the maintenance of individual and community. Where this end is achieved, the precept ceases to have any meaning. Moreover, it holds only for the race, not for every individual. It does not apply to anyone who can live without labour on his possessions, and of course contemplation, as a spiritual form of action in the Kingdom of God, takes precedence over the commandment in its literal sense. Moreover, for the popular theology of the time, the highest form of monastic productivity lay in the increase of the *Thesaurus ecclesie* through prayer and chant.

Now only do these exceptions to the duty to labour naturally no longer hold for Baxter, but he holds most emphatically that wealth does not exempt anyone from the unconditional command. Even the wealthy shall not eat without working, for even though they do not need to labour to support their own needs, there is God's commandment which they, like the poor, must obey. For everyone without exception God's Providence has prepared a calling, which he should profess and in which he should labour. And this calling is not, as it was for the Lutheran, a fate to which he must submit and which he must make the best of, but God's commandment to the individual to work for the divine glory. This seemingly subtle difference had far-reaching psychological consequences, and became connected with a further development of the providential interpretation of the economic order which had begun in scholasticism.

The phenomenon of the division of labour and occupations in society had, among others, been interpreted by Thomas Aquinas, to whom we may most conveniently refer, as a direct consequence of the divine scheme of things. But the places assigned to each man in this cosmos follow *ex causis naturalibus* and are fortuitous (contingent in the Scholastic terminology). The differentiation of men into the classes and occupations established through historical development became for Luther, as we have seen, a direct result of the divine will. The perseverance of the individual in the place and within the limits which God had assigned to him was a religious duty. This was the more certainly the consequence since the relations of Lutheranism to the world were in general uncertain from the beginning and remained so. Ethical principles for the reform of the world could not be found in Luther's realm of ideas; in fact it never quite freed itself from Pauline indifference. Hence the world had to be accepted as it was, and this alone could be made a religious duty. But in the Puritan view, the providential character of the play of private economic interests takes on a somewhat different emphasis. True to the Puritan tendency to pragmatic interpretations, the providential purpose of the division of labour is to be known by its fruits. On this point Baxter expresses himself in terms which more than once directly recall Adam Smith's well-known apotheosis of the division of labour. The specialization of occupations leads, since it makes the development of skill possible, to a quantitative and qualitative improvement in production, and thus serves the common good, which is identical with the good of the greatest possible number. So far, the motivation is purely utilitarian, and is closely related to the customary viewpoint of much of the secular literature of the time.

But the characteristic Puritan element appears when Baxter sets at the head of his discussion the statement that "outside of a well-marked calling the accomplishments of a man are only casual and irregular, and he spends more time in idleness than at work", and when he concludes it as follows: "and he [the specialized worker] will carry out his work in order while another remains in constant confusion, and his business knows neither time nor place ... therefore is a certain calling the best for everyone." Irregular work, which the ordinary labourer is often forced to accept, is often unavoidable, but always an unwelcome state of transition. A man without a calling thus lacks the systematic, methodical character which is, as we have seen, demanded by worldly asceticism.

The Quaker ethic also holds that a man's life in his calling is an exercise in ascetic virtue, a proof of his state of grace through his conscientiousness, which is expressed in the care and method with which he pursues his calling. What God demands is not labour in itself, but rational labour in a calling. In the Puritan concept of the calling the emphasis is always placed on this methodical character of worldly asceticism, not, as with Luther, on the acceptance of the lot which God has irretrievably assigned to man.

Hence the question whether anyone may combine several callings is answered in the affirmative, if it is useful for the common good or one's own, and not injurious to anyone, and if it does not lead to unfaithfulness in one of the callings. Even a change of calling is by no means regarded as objectionable, if it is not thoughtless and is made for the purpose of pursuing a calling more pleasing to God, which means, on general principles, one more useful. It is true that the usefulness of a calling, and thus its favour in the sight of God, is measured primarily in moral terms, and thus in terms of the importance of the goods produced in it for the community. But a further, and, above all, in practice the most important, criterion is found in private profitableness. For if that God, whose hand the Puritan sees in all the occurrences of life, shows one of His elect a chance of profit, he must do it with a purpose. Hence the faithful Christian must follow the call by taking advantage of the opportunity. "If God show you a way in which you may lawfully get more than in another way (without wrong to your soul or to any other), if you refuse this, and choose the less gainful way, you cross one of the ends of your calling, and you refuse to be God's steward, and to accept His gifts and use them for Him, when He requireth it: you may labour to be rich for God, though not for the flesh and sin."

Wealth is thus bad ethically only in so far as it is a temptation to idleness and sinful enjoyment of life, and its acquisition is bad only when it is with the purpose of later living merrily and without care. But as a performance of duty in a calling it is not only morally permissible, but actually enjoined. The parable of the servant who was rejected because he did not increase the talent which was entrusted to him seemed to say so directly. To wish to be poor was, it was often argued, the same as wishing to be unhealthy; it is objectionable as a glorification of works and derogatory to the glory of God. Especially begging, on the part of one able to work, is not only the sin of slothfulness, but a violation of the duty of brotherly love according to the Apostle's own word. The emphasis on the ascetic importance of a fixed calling provided an ethical justification of the modern specialized division of labour. In a similar way the providential interpretation of profit-making justified the activities of the business man. The superior indulgence of the seigneur and the parvenu ostentation of the *nouveau riche* are equally detestable to asceticism.

Well crafted to keep people in line

But, on the other hand, it has the highest ethical appreciation of the sober, middle-class, self-made Man. "God blesseth His trade" is a stock remark about those good men who had successfully followed the divine hints. The whole power of the God of the Old Testament, who rewards His people for their obedience in this life, necessarily exercised a similar influence on the Puritan who, following Baxter's advice, compared his own state of grace with that of the heroes of the Bible, and in the process interpreted the statements of the Scriptures as the articles of a book of statutes.

Of course, the words of the Old Testament were not entirely without ambiguity. We have seen that Luther first used the concept of the calling in the secular sense in translating a passage from Jesus Sirach. But the book of Jesus Sirach belongs, with the whole atmosphere expressed in it, to those parts of the broadened Old Testament with distinctly traditionalistic tendency, in spite of Hellenistic influences. It is characteristic that down to the present day this book seems to enjoy a special favour among Lutheran German peasants just as the Lutheran influence in large sections of German Pietism has been expressed by a preference for Jesus Sirach.

The Puritans repudiated the Apocrypha as not inspired, consistently with their sharp distinction between things divine and things of the flesh. But among the canonical books that of Job had all the more influence. On the one hand it contained a grand conception of the absolute sovereign majesty, of God, beyond all human comprehension, which was closely related to that of Calvinism. With that, on the other hand, it combined the certainty which, though incidental for Calvin, came to be of great importance for Puritanism, that God would bless His own in this life – in the book of Job only – and also in the material sense. The Oriental quietism, which appears in several of the finest verses of the Psalms and in the Proverbs, was interpreted away, just as Baxter did with the traditionalistic tinge of the passage in the 1st Epistle to the Corinthians, so important for the idea of the calling.

But all the more emphasis was placed on those parts of the Old Testament which praise formal legality as a sign of conduct pleasing to God. They held the theory that the Mosaic Law had only lost its validity through Christ in so far as it contained ceremonial or purely historical precepts applying only to the Jewish people, but that otherwise it had always been valid as an expression of the natural law, and must hence be retained. This made it possible, on the one hand, to eliminate elements which could not be reconciled with modern life. But still, through its numerous related features, Old Testament morality was able to give a powerful impetus to that spirit of self-righteous and sober legality which was so characteristic of the worldly asceticism of this form of Protestantism.

Thus when authors, as was the case with several contemporaries as well as later writers, characterize the basic ethical tendency of Puritanism, especially in England, as English Hebrews they are, correctly understood, not wrong. It is necessary, however, not to think of Palestinian Judaism at the time of the writing of the Scriptures, but of Judaism as it became under the influence of many centuries of formalistic, legalistic, and Talmudic education. Even then one must be very careful in drawing parallels. The general tendency of the older Judaism toward a naive acceptance of life as such was far removed from the special characteristics of Puritanism. It was, however, just as far – and this ought not to be overlooked – from the economic ethics of mediaeval and modern Judaism, in the traits which determined the positions of both in the development of the capitalistic ethos. The Jews stood on the side of the politically and speculatively oriented adventurous capitalism; their ethos was, in a word, that of pariah-capitalism. But Puritanism carried the ethos of the rational organization of capital and labour. It took over from the Jewish ethic only what was adapted to this purpose.

(Skimming)

To analyse the effects on the character of peoples of the penetration of life with Old Testament norms – a tempting task which, however, has not yet satisfactorily been done even for Judaism – would be impossible within the limits of this sketch. In addition to the relationships already pointed out, it is important for the general inner attitude of the Puritans, above all, that the belief that they were God's chosen people saw in them a great renaissance. Even the kindly Baxter thanked God that he was born in England, and thus in the true Church, and nowhere else. This thankfulness for one's own perfection by the grace of God penetrated the attitude toward life of the Puritan middle class, and played its part in developing that formalistic, hard, correct character which was peculiar to the men of that heroic age of capitalism.

Let us now try to clarify the points in which the Puritan idea of the calling and the premium it placed upon ascetic conduct was bound directly to influence the development of a capitalistic way of life. As we have seen, this asceticism turned with all its force against one thing: the spontaneous enjoyment of life and all it had to offer. This is perhaps most characteristically brought out in the struggle over the Book of Sports which James I and Charles I made into law expressly as a means of counteracting Puritanism, and which the latter ordered to be read from all the pulpits. The fanatical opposition of the Puritans to the ordinances of the King, permitting certain popular amusements on Sunday outside of Church hours by law, was not only explained by the disturbance of the Sabbath rest, but also by resentment against the intentional diversion from the ordered life of the saint, which it caused. And, on his side, the King's threats of severe punishment for every attack on the legality of those sports were motivated by his purpose of breaking the anti-authoritarian ascetic tendency of Puritanism, which was so dangerous to the State. The feudal and monarchical forces protected the pleasure seekers against the rising middle-class morality and the anti-authoritarian ascetic conventicles, just as today capitalistic society tends to protect those willing to work against the class morality of the proletariat and the anti-authoritarian trade union.

As against this the Puritans upheld their decisive characteristic, the principle of ascetic conduct. For otherwise the Puritan aversion to sport, even for the Quakers, was by no means simply one of principle. Sport was accepted if it served a rational purpose, that of recreation necessary for physical efficiency. But as a means for the spontaneous expression of undisciplined impulses, it was under suspicion; and in so far as it became purely a means of enjoyment, or awakened pride, raw instincts or the irrational gambling instinct, it was of course strictly condemned. Impulsive enjoyment of life, which leads away both from work in a calling and from religion, was as such the enemy of rational asceticism, whether in the form of seigneurial sports, or the enjoyment of the dance-hall or the public-house of the common man.

Its attitude was thus suspicious and often hostile to the aspects of culture without any immediate religious value. It is not, however, true that the ideals of Puritanism implied a solemn, narrow-minded contempt of culture. Quite the contrary is the case at least for science, with the exception of the hatred of Scholasticism. Moreover, the great men of the Puritan movement were thoroughly steeped in the culture of the Renaissance. The sermons of the Presbyterian divines abound with classical allusions and even the Radicals, although they objected to it, were not ashamed to display that kind of learning in theological polemics. Perhaps no country was ever so full of graduates as New England in the first generation of its existence. The satire of their opponents, such as, for instance, Butler's *Hudibras*, also attacks primarily the pedantry and highly trained dialectics of the Puritans. This is partially due to the religious valuation of knowledge which followed from their attitude to the Catholic *fides implicita*.

But the situation is quite different when one looks at non-scientific literature and especially the fine arts. Here asceticism descended like a frost on the life of "Merrie old England." And not only worldly merriment felt its effect. The Puritan's ferocious hatred of everything which smacked of superstition, of all survivals of magical or sacramental salvation, applied to the Christmas festivities and the May Pole and all spontaneous religious art. That there was room in Holland for a great, often uncouthly realistic art proves only how far from completely the authoritarian moral discipline of that country was able to counteract the influence of the court and the regents (a class of rentiers), and also the joy in life of the parvenu bourgeoisie, after the short supremacy of the Calvinistic theocracy had been transformed into a moderate national Church, and with it Calvinism had perceptibly lost in its power of ascetic influence.

The theatre was obnoxious to the Puritans, and with the strict exclusion of the erotic and of nudity from the realm of toleration, a radical view of either literature or art could not exist. The conceptions of idle talk, of superfluities, and of vain ostentation, all designations of an irrational attitude without objective purpose, thus not ascetic, and especially not serving the glory of God, but of man, were always at hand to serve in deciding in favour of sober utility as against any artistic tendencies. This was especially true in the case of decoration of the person, for instance clothing. That powerful tendency toward uniformity of life, which today so immensely aids the capitalistic interest in the standardization of production, had its ideal foundations in the repudiation of all idolatry of the flesh.

Of course we must not forget that Puritanism included a world of contradictions, and that the instinctive sense of eternal greatness in art was certainly stronger among its leaders than in the atmosphere of the Cavaliers. Moreover, a unique genius like Rembrandt, however little his conduct may have been acceptable to God in the eyes of the Puritans, was very strongly influenced in the character of his work by his religious environment. But that does not alter the picture as a whole. In so far as the development of the Puritan tradition could, and in part did, lead to a powerful spiritualization of personality, it was a decided benefit to literature. But for the most part that benefit only accrued to later generations.

Although we cannot here enter upon a discussion of the influence of Puritanism in all these directions, we should call attention to the fact that the toleration of pleasure in cultural goods, which contributed to purely aesthetic or athletic enjoyment, certainly always ran up against one characteristic limitation: they must not cost anything. Man is only a trustee of the goods which have come to him through God's grace. He must, like the servant in the parable, give an account of every penny entrusted to him, and it is at least hazardous to spend any of it for a purpose which does not serve the glory of God but only one's own enjoyment. What person, who keeps his eyes open, has not met representatives of this viewpoint even in the present? The idea of a man's duty to his possessions, to which he subordinates himself as an obedient steward, or even as an acquisitive machine, bears with chilling weight on his life. The greater the possessions the heavier, if the ascetic attitude toward life stands the test, the feeling of responsibility for them, for holding them undiminished for the glory of God and increasing them by restless effort. The origin of this type of life also extends in certain roots, like so many aspects of the spirit of capitalism, back into the Middle Ages. But it was in the ethic of ascetic Protestantism that it first found a consistent ethical foundation. Its significance for the development of capitalism is obvious. This worldly Protestant asceticism, as we may recapitulate up to this point, acted powerfully against the spontaneous enjoyment of possessions; it restricted consumption, especially of luxuries. On the other hand, it had the psychological effect of freeing the acquisition of goods from the inhibitions of traditionalistic ethics. It broke the bonds of the impulse of acquisition in that it not only legalized it, but (in the sense discussed) looked upon it as directly willed by God. The campaign against the temptations of the flesh, and the dependence on external things, was, as besides the Puritans the great Quaker apologist Barclay expressly says, not a struggle against the rational acquisition, but against the irrational use of wealth.

But this irrational use was exemplified in the outward forms of luxury which their code condemned as idolatry of the flesh, however natural they had appeared to the feudal mind. On the other hand, they approved the rational and utilitarian uses of wealth which were willed by God for the needs of the individual and the community. They did not wish to impose mortification on the man of wealth, but the use of his means for necessary and practical things. The idea of comfort characteristically limits the extent of ethically permissible expenditures. It is naturally no accident that the development of a manner of living consistent with that idea may be observed earliest and most clearly among the most consistent representatives of this whole attitude toward life. Over against the glitter and ostentation of feudal magnificence which, resting on an unsound economic basis, prefers a sordid elegance to a sober simplicity, they set the clean and solid comfort of the middle-class home as an ideal.

On the side of the production of private wealth, asceticism condemned both dishonesty and impulsive avarice. What was condemned as covetousness, Mammonism, etc., was the pursuit of riches for their own sake. For wealth in itself was a temptation. But here asceticism was the power "which ever seeks the good but ever creates evil"; what was evil in its sense was possession and its temptations. For, in conformity with the Old Testament and in analogy to the ethical valuation of good works, asceticism looked upon the pursuit of wealth as an end in itself as highly reprehensible; but the attainment of it as a fruit of labour in a calling was a sign of God's blessing. And even more important: the religious valuation of restless, continuous, systematic work in a worldly calling, as the highest means to asceticism, and at the same time the surest and most evident proof of rebirth and genuine faith, must have been the most powerful conceivable lever for the expansion of that attitude toward life which we have here called the spirit of capitalism.

When the limitation of consumption is combined with this release of acquisitive activity, the inevitable practical result is obvious: accumulation of capital through ascetic compulsion to save. The restraints which were imposed upon the consumption of wealth naturally served to increase it by making possible the productive investment of capital. How strong this influence was is not, unfortunately, susceptible to exact statistical demonstration. In New England the connection is so evident that it did not escape the eye of so discerning a historian as Doyle. But also in Holland, which was really only dominated by strict Calvinism for seven years, the greater simplicity of life in the more seriously religious circles, in combination with great wealth, led to an excessive propensity to accumulation.

That, furthermore, the tendency which has existed everywhere and at all times, being quite strong in Germany today, for middle-class fortunes to be absorbed into the nobility, was necessarily checked by the Puritan antipathy to the feudal way of life, is evident. English Mercantilist writers of the seventeenth century attributed the superiority of Dutch capital to English to the circumstance that newly acquired wealth there did not regularly seek investment in land. Also, since it is not simply a question of the purchase of land, it did not there seek to transfer itself to feudal habits of life, and thereby to remove itself from the possibility of capitalistic investment. The high esteem for agriculture as a peculiarly important branch of activity, also especially consistent with piety, which the Puritans shared, applied (for instance in Baxter) not to the landlord, but to the yeoman and farmer, in the eighteenth century not to the squire, but the rational cultivator. Through the whole of English society in the time since the seventeenth century goes the conflict between the squirearchy, the representatives of "merrie old England," and the Puritan circles of widely varying social influence. Both elements, that of an unspoiled naive joy of life, and of a strictly regulated, reserved self-control, and conventional ethical conduct are even today combined to form the English national character. Similarly, the early history of the North American Colonies is dominated by the sharp contrast of the adventurers, who wanted to set up plantations with the labour of indentured servants, and live as feudal lords, and the specifically middle-class outlook of the Puritans.

As far as the influence of the Puritan outlook extended, under all circumstances – and this is, of course, much more important than the mere encouragement of capital accumulation – it favoured the development of a rational bourgeois economic life; it was the most important, and above all the only consistent influence in the development of that life. It stood at the cradle of the modern economic man.

To be sure, these Puritanical ideals tended to give way under excessive pressure from the temptations of wealth, as the Puritans themselves knew very well. With great regularity we find the most genuine adherents of Puritanism among the classes which were rising from a lowly status, the small bourgeois and farmers, while the *beati possidentes*, even among Quakers, are often found tending to repudiate the old ideals. It was the same fate which again and again befell the predecessor of this worldly asceticism, the monastic asceticism of the Middle Ages. In the latter case, when rational economic activity had worked out its full effects by strict regulation of conduct and limitation of consumption, the wealth accumulated either succumbed directly to the nobility, as in the time before the Reformation, or monastic discipline threatened to break down, and one of the numerous reformations became necessary.

In fact the whole history of monasticism is in a certain sense the history of a continual struggle with the problem of the secularizing influence of wealth. The same is true on a grand scale of the worldly asceticism of Puritanism. The great revival of Methodism, which preceded the expansion of English industry toward the end of the eighteenth century, may well be compared with such a monastic reform. We may hence quote here a passage from John Wesley himself which might well serve as a motto for everything which has been said above. For it shows that the leaders of these ascetic movements understood the seemingly paradoxical relationships which we have here analysed perfectly well, and in the same sense that we have given them. He wrote:

> "I fear, wherever riches have increased, the essence of religion has decreased in the same proportion. Therefore I do not see how it is possible, in the nature of things, for any revival of true religion to continue long. For religion must necessarily produce both industry and frugality, and these cannot but produce riches. But as riches increase, so will pride, anger, and love of the world in all its branches. How then is it possible that Methodism, that is, a religion of the heart, though it flourishes now as a green bay tree, should continue in this state? For the Methodists in every place grow diligent and frugal; consequently they increase in goods. Hence they proportionately increase in pride, in anger, in the desire of the flesh, the desire of the eyes, and the pride of life. So, although the form of religion remains, the spirit is swiftly vanishing away. Is there no way to prevent this – this continual decay of pure religion? We ought not to prevent people from being diligent and frugal; we must exhort all Christians to gain all they can, and to save all they can; that is, in effect, to grow rich."

people attached more to materialistic

There follows the advice that those who gain all they can and save all they can should also give all they can, so that they will grow in grace and lay up a treasure in heaven. It is clear that Wesley here expresses, even in detail, just what we have been trying to point out. As Wesley here says, the full economic effect of those great religious movements, whose significance for economic development lay above all in their ascetic educative influence, generally came only after the peak of the purely religious enthusiasm was past. Then the intensity of the search for the Kingdom of God commenced gradually to pass over into sober economic virtue; the religious roots died out slowly, giving way to utilitarian worldliness. Then, as Dowden puts it, as in Robinson Crusoe, the isolated economic man who carries on missionary activities on the side takes the place of the lonely spiritual search for the Kingdom of Heaven of Bunyan's pilgrim, hurrying through the market-place of Vanity. When later the principle "to make the most of both worlds" became dominant in the end, as Dowden has remarked, a good conscience simply became one of the means of enjoying a comfortable bourgeois life, as is well expressed in the German proverb about the soft pillow. What the great religious epoch of the seventeenth century bequeathed to its utilitarian successor was, however, above all an amazingly good, we may even say a pharisaically good, conscience in the acquisition of money, so long as it took place legally. Every trace of the *deplacere vix potest* has disappeared.

A specifically bourgeois economic ethic had grown up. With the consciousness of standing in the fullness of God's grace and being visibly blessed by Him, the bourgeois business man, as long as he remained within the bounds of formal correctness, as long as his moral conduct was spotless and the use to which he put his wealth was not objectionable, could follow his pecuniary interests as he would and feel that he was fulfilling a duty in doing so. The power of religious asceticism provided him in addition with sober, conscientious, and unusually industrious workmen, who clung to their work as to a life purpose willed by God.

Finally, it gave him the comforting assurance that the unequal distribution of the goods of this world was a special dispensation of Divine Providence, which in these differences, as in particular grace, pursued secret ends unknown to men. Calvin himself had made the much-quoted statement that only when the people, i.e. the mass of labourers and craftsmen, were poor did they remain obedient to God. In the Netherlands (Pieter de la Court and others), that had been secularized to the effect that the mass of men only labour when necessity forces them to do so. This formulation of a leading idea of capitalistic economy later entered into the current theories of the productivity of low wages. Here also, with the dying out of the religious root, the utilitarian interpretation crept in unnoticed, in the line of development which we have again and again observed. Mediaeval ethics not only tolerated begging but actually glorified it in the mendicant orders. Even secular beggars, since they gave the person of means opportunity for good works through giving alms, were sometimes considered an estate and treated as such. Even the Anglican social ethic of the Stuarts was very close to this attitude. It remained for Puritan Asceticism to take part in the severe English Poor Relief Legislation which fundamentally changed the situation. And it could do that because the Protestant sects and the strict Puritan communities actually did not know any begging in their own midst.

On the other hand, seen from the side of the workers, the Zinzendorf branch of Pietism, for instance, glorified the loyal worker who did not seek acquisition, but lived according to the apostolic model, and was thus endowed with the charisma of the disciples. Similar ideas had originally been prevalent among the Baptists.

Now naturally the whole ascetic literature of almost all denominations is saturated with the idea that faithful labour, even at low wages, on the part of those whom life offers no other opportunities, is highly pleasing to God. In this respect Protestant Asceticism added in itself nothing new. But it not only deepened this idea most powerfully, it also created the force which was alone decisive for its effectiveness: the psychological sanction of it through the conception of this labour as a calling, as the best, often in the last analysis the only means of attaining certainty of grace. And on the other hand it legalized the exploitation of this specific willingness to work, in that it also interpreted the employer's business activity as a calling. It is obvious how powerfully the exclusive search for the Kingdom of God only through the fulfilment of duty in the calling, and the strict asceticism which Church discipline naturally imposed, especially on the propertyless classes, was bound to affect the productivity of labour in the capitalistic sense of the word. The treatment of labour as a calling became as characteristic of the modern worker as the corresponding attitude toward acquisition of the business man. It was a perception of this situation, new at his time, which caused so able an observer as Sir William Petty to attribute the economic power of Holland in the seventeenth century to the fact that the very numerous dissenters in that country (Calvinists and Baptists) "are for the most part thinking, sober men, and such as believe that Labour and Industry is their duty towards God".

Calvinism opposed organic social organization in the fiscal-monopolistic form which it assumed in Anglicanism under the Stuarts, especially in the conceptions of Laud, this alliance of Church and State with the monopolists on the basis of a Christian, social ethical foundation. Its leaders were universally among the most passionate opponents of this type of politically privileged commercial, putting-out, and colonial capitalism. Over against it they placed the individualistic motives of rational legal acquisition by virtue of one's own ability and initiative. And, while the politically privileged monopoly industries in England all disappeared in short order, this attitude played a large and decisive part in the development of the industries which grew up in spite of and against the authority of the State. The Puritans (Prynne, Parker) repudiated all connection with the large-scale capitalistic courtiers and projectors as an ethically suspicious class. On the other hand, they took pride in their own superior middle-class business morality, which formed the true reason for the persecutions to which they were subjected on the part of those circles. Defoe proposed to win the battle against dissent by boycotting bank credit and withdrawing deposits. The difference of the two types of capitalistic attitude went to a very large extent hand in hand with religious differences. The opponents of the Nonconformists, even in the eighteenth century, again and again ridiculed them for personifying the spirit of shopkeepers, and for having ruined the ideals of old England. Here also lay the difference of the Puritan economic ethic from the Jewish; and contemporaries (Prynne) knew well that the former and not the latter was the bourgeois capitalistic ethic.

One of the fundamental elements of the spirit of modern capitalism, and not only of that but of all modern culture: rational conduct on the basis of the idea of the calling, was born – that is what this discussion has sought to demonstrate – from the spirit of Christian asceticism. One has only to re-read the passage from Franklin, quoted at the beginning of this essay, in order to see that the essential elements of the attitude which was there called the spirit of capitalism are the same as what we have just shown to be the content of the Puritan worldly asceticism, only without the religious basis, which by Franklin's time had died away. The idea that modern labour has an ascetic character is of course not new. Limitation to specialized work, with a renunciation of the Faustian universality of man which it involves, is a condition of any valuable work in the modern world; hence deeds and renunciation inevitably condition each other today. This fundamentally ascetic trait of middle-class life, if it attempts to be a way of life at all, and not simply the absence of any, was what Goethe wanted to teach, at the height of his wisdom, in the *Wanderjahren*, and in the end which he gave to the life of his Faust. For him the realization meant a renunciation, a departure from an age of full and beautiful humanity, which can no more be repeated in the course of our cultural development than can the flower of the Athenian culture of antiquity.

The Puritan wanted to work in a calling; we are forced to do so. For when asceticism was carried out of monastic cells into everyday life, and began to dominate worldly morality, it did its part in building the tremendous cosmos of the modern economic order. This order is now bound to the technical and economic conditions of machine production which today determine the lives of all the individuals who are born into this mechanism, not only those directly concerned with economic acquisition, with irresistible force. Perhaps it will so determine them until the last ton of fossilized coal is burnt. In Baxter's view the care for external goods should only lie on the shoulders of the "saint like a light cloak, which can be thrown aside at any moment." But fate decreed that the cloak should become an iron cage.

Since asceticism undertook to remodel the world and to work out its ideals in the world, material goods have gained an increasing and finally an inexorable power over the lives of men as at no previous period in history. Today the spirit of religious asceticism – whether finally, who knows? – has escaped from the cage. But victorious capitalism, since it rests on mechanical foundations, needs its support no longer. The rosy blush of its laughing heir, the Enlightenment, seems also to be irretrievably fading, and the idea of duty in one's calling prowls about in our lives like the ghost of dead religious beliefs. Where the fulfilment of the calling cannot directly be related to the highest spiritual and cultural values, or when, on the other hand, it need not be felt simply as economic compulsion, the individual generally abandons the attempt to justify it at all. In the field of its highest development, in the United States, the pursuit of wealth, stripped of its religious and ethical meaning, tends to become associated with purely mundane passions, which often actually give it the character of sport.

No one knows who will live in this cage in the future, or whether at the end of this tremendous development, entirely new prophets will arise, or there will be a great rebirth of old ideas and ideals, or, if neither, mechanized petrification, embellished with a sort of convulsive self-importance. For of the fast stage of this cultural development, it might well be truly said: "Specialists without spirit, sensualists without heart; this nullity imagines that it has attained a level of civilization never before achieved."

But this brings us to the world of judgments of value and of faith, with which this purely historical discussion need not be burdened. The next task would be rather to show the significance of ascetic rationalism which has only been touched in the foregoing sketch for the content of practical social ethics, thus for the types of organization and the functions of social groups from the conventicle to the State. Then its relations to humanistic rationalism, its ideals of life and cultural influence; further to the development of philosophical and scientific empiricism, to technical development and to spiritual ideals would have to be analysed. Then its historical development from the mediaeval beginnings of worldly asceticism to its dissolution into pure utilitarianism would have to be traced out through all the areas of ascetic religion. Only then could the quantitative cultural significance of ascetic Protestantism in its relation to the other plastic elements of modern culture be estimated.

Here we have only attempted to trace the fact and the direction of its influence to their motives in one, though a very important point. But it would also further be necessary to investigate how Protestant Asceticism was in turn influenced in its development and its character by the totality of social conditions, especially economic. The modern man is in general, even with the best will, unable to give religious ideas a significance for culture and national character which they deserve. But it is, of course, not my aim to substitute for a one-sided materialistic an equally one-sided spiritualistic causal interpretation of culture and of history. Each is equally possible, but each, if it does not serve as the preparation, but as the conclusion of an investigation, accomplish equally little in the interest of historical truth.

Max Weber Archive | Table of Contents

Asceticism "Greek exercise or training"
L lifestyle from abstinance from worldly pleasure, usually for religious + spiritual goals

14.72

10/24

Exam Review + Weber

Hand back exams
at end

but go over now
papers as well

Guidelines for Essay / Exams

Identification Qu - Weaker part
easy pts
Wild guesses don't work
Give defn + which Author

(+)/(−) freedom
(−) Absence of coercision : Friedman
(+) Specific meaning given to freedom : Rand

Spend more time on identifing key concepts from
each author

②

~~Don't~~

Essay - don't define all you know about Marx/capitalism

Organize your plan/outline

~~The outline is also~~

find the cohesion

announce how you are studying in intro

Role of family - didn't talk about in class

So specific sub qu

Use specific examples

- diff b/w avg + good essay
- ~~to mo~~ try to find
- Moral standard: fetishism & Commodity
  tells us about Marx's attitude
- family: Rand mention how used Dominique
  and their couple-ship vs w/ others

(3)

Essay 1 Moral standards

don't need all statements on econ
but diff lense they look at
freedom vs equality
↑ ↑
Friedman Marx

Marx: ⊕ freedom
Friedman: ⊖ freedom (silly abstraction)

Sci views: how they think market operates
role of gov
Friedman: protect freedom
Marx: ally of borgiouse

Essay 3 Class + Class Conflict w/ Neoliberal view

don't say anything explicitly
markets that should be free become unfree

(4)

inheritance → produce of inequality

Consequence to children
diff inital capital
don't start the same

inside class hard to move up
Friedman mentions this a
Static view moving
movements up or down

Prof: Don't be nervous to start answering the qu

Grade dist
This exam pratice for final
So not suprised by final
if final ≥ midterm, drop midterm

$\frac{56\ (2x)}{60}$

28, 31, 34, 37

39, 42, 43, 47, 52

(5)

Spirit of Capitalism

Moving to 3d paradigm

Marx: big dicodomy b/w material world + world of ideas

- base, superstiture

Marx superstructure ← base drives

These authors superstructure → base reflects set of ideas

ideas reflect reality - more than determining reality

Weber - focuses on ideas of key of Understanding how the world works

6

But what is the problem he is trying to solve?

How do we get here?
Who cares about it?

Where does capitalism come from?

Neoclassical: Me: Materialistic sense
Joey: Limited Resources + Unlimited demands
Nature

Prof: So capitalism natural response

Marx: Comes out of history

Prof: Can you get capitalism in all times + all places?
Is it universal?

Joey: Friedman: Need certain contracts in place
Prof: But could have those institutionals anywhere

7

Weber: Capitalism is unnatural

Bizare humans want material change

The thought natural: backward bending supply curve

Above a certain pt, people start to value other things (friends, family)

People obsessed w/ $ + work all the time

(missed some)

Prof: Need transformation that produces this

What spirit of capitalism is about?

Is capitalism just about making $?

Can Mafia + Drug lords produce capitalism?

Do they have organization

Rationalization

Moral / Ethical standard

8

things which enhance the glory of god

Drug cartels: very organized

but little moral framework

Soviet Union: internal visas needed

take the night train

Come back that night

So no passport needed

Pione at conferce ~~to visit the~~ at end of

Soviet Union

visited Leningrad

Professor arranged transportation

That time of year lots of busses

tried to hire one

~~Took~~ said ~~that~~ bus broke down - to garage

Picked up kids in the rain

Isn't capitalism wonderful?

(9)

* Can only have capitalism if have long term contracts

So need moral / legal framework where people respect long term conflicts

Need a rational framework

Can't just profit any old way

Must escape old / natural ways

Traditional framework: family values

- constrain on capitalism
- So must move productive area outside the family
- need sep industrial space

Mexico → no seperation b/w work + family

didn't see productive facility as 2nd operation

So hard to org in efficent way

(10)

Finances of household + biz mixed

Working capital spent on hospital bills

Could not start to figure out efficency

So must seperate household + biz

So escape committments to family

Distinctions not natural

More natural : family than biz

World partly rational + partly magical

Weber : economic development

- emergence of modern econ is a problem
- diff from conventual liberalism

Sol : Protirestasm

(left 30 min early)

Ted's Notes

14.72 10-24-2012

further passed through (3:25) I left at 3:~~30~~ 35
concept;

1) — Capitalism requires ability to form long-term contracts.

(story about Russian bus tour (KOE))
→ "Isn't capitalism wonderful?"

I separation biz + family

2) — Capitalism requires overcoming traditional modes of labor, business and life

— productive activity is shifted from family business to institutional space, and scale/accumulation is prioritized over needs fulfillment and other ideals

shifted family business

[illegible] — sole proprietorships — no natural separation, unlike a corporation with its own separate identity.

distinctions
Weber argues that such ~~distinctions~~
are not natural.
But reason itself is ~~[illegible]~~ in some
sense unnatural

Capitalism requires this separate business
realm, conventions, its own
moral system that values
things like fiduciary duty
and enforcement of long-term
contracts over things like
family, lifestyle, health

not in family
piece rate shop

~ ~

Weber — superstructure influencing base — Puritan ethic

← That is the superstructure?

"I think it is funny, but I don't think Weber has a sense of humor. He's German — er well, I mean, he's very serious."

Puritanism is not the only consistent system for ~~~~ supporting a capitalist ethic, but it is a particularly good one.

capitalist ethic

An alternative: Rand & similar worldviews what Webber said BF?

Capitalism

"Spirit of Capitalism"

Protestantism

necessary

one means, alternatives include e.g. productive creativity

e.g. Benjamin Franklin

but he is not a Protestant

?the non protestent alt

"Essentially we're solving an identification problem — Franklin allows us to isolate the spirit of capitalism from both protestantism and capitalism per se*

identification problem- Franklin trys to isolate the spirit of capitalism from both protistm + capitalism

But this is also separate from capitalism because

It is a bit bizarre that the notion of predestination leads to this system

This all doesn't add up

Now if you look at ~~[illegible]~~ Puritanism — they believe in predestination, but are obsessed with fear of damnation, which led them to be constantly searching for signs of their own salvation. Silly

Weber constructs a compelling / elegant argument. He also clearly illustrates how thoroughly ideas drove socioeconomic systems.

Weber: 'People are driven by material (one: arguably emotional/Maslow needs, too) self interest, but ideas are like switchmen, guiding the train along a particular course in doing so.'

Weber — but the Protestant ethic is gone now. God is dead.

The ~~[illegible]~~ Puritans wanted to work in a calling — asceticism came out of everyday life and into social/economic systems.

calling

And there's a spirit drove them, but that spirit no longer exists sometimes. The mechanism itself keeps it in place.

It's self-sustaining

Next assignment: Polanyi

- a different perspective, but one in which likewise ideas are again the driving force, not material things.

Next paper: analyze 2 (or 3) generations of your family's ~~[illegible]~~ work history and ~~[illegible]~~ determine which of the frameworks we've examined are most useful in ~~[illegible]~~ the analysis.

"It's certainly a lot more interesting to read than essays about The Fountainhead."

10/28
LA

Ted - particularly well linked
Capitalism + Protestism

Working -> end its itself

Me: Like you w/ $
Ted: I'm doing it for freedom
They doing since obligated
Under terms of religion
Local community

Puritan particular ~~gd~~ good version of it
~~Dutch~~ Italians lazy
Dutch + Jews ~~&~~ ← religion only one didn't charge interest
adventures kill them all

Ted + I Everyone is long + pretentious
Could be much more precise

John Maynard Keynes

Read 10/28

From Wikipedia, the free encyclopedia

John Maynard Keynes, 1st Baron Keynes,[1] CB FBA (/ˈkeɪnz/ *KAYNZ*; 5 June 1883 – 21 April 1946) was a British economist whose ideas have profoundly affected the theory and practice of modern macroeconomics, and informed the economic policies of governments. He built on and refined earlier work on the causes of business cycles, and advocated the use of fiscal and monetary measures to mitigate the adverse effects of economic recessions and depressions. Keynes is widely considered to be one of the founders of modern macroeconomics, and the most influential economist of the 20th century.[2][3][4][5] His ideas are the basis for the school of thought known as Keynesian economics, as well as its various offshoots.

In the 1930s, Keynes spearheaded a revolution in economic thinking, overturning the older ideas of neoclassical economics that held that free markets would, in the short to medium term, automatically provide full employment, as long as workers were flexible in their wage demands. Keynes instead argued that aggregate demand determined the overall level of economic activity, and that inadequate aggregate demand could lead to prolonged periods of high unemployment. Following the outbreak of World War II, Keynes's ideas concerning economic policy were adopted by leading Western economies. During the 1950s and 1960s, the success of Keynesian economics resulted in almost all capitalist governments adopting its policy recommendations.

more of a self help

Democratic

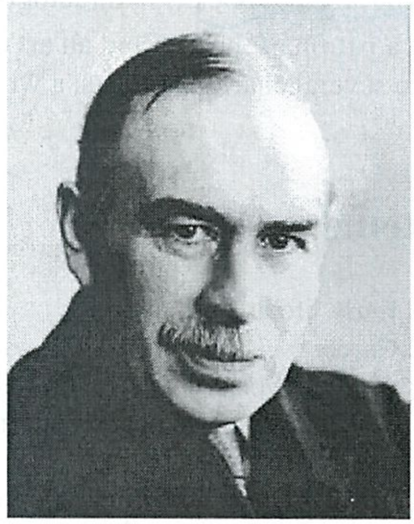
Keynes's influence waned in the 1970s, partly as a result of problems that began to afflict the Anglo-American economies from the start of the decade, and partly because of critiques from Milton Friedman and other economists who were pessimistic about the ability of governments to regulate the business cycle with fiscal policy.[6] However, the advent of the global financial crisis in 2007 caused a resurgence in Keynesian thought. Keynesian economics provided the theoretical underpinning for economic policies undertaken in response to the crisis by Presidents George W. Bush and Barack Obama of the United States, Prime Minister Gordon Brown of the United Kingdom, and other heads of governments.[7]

Conservative resergance

keysian resogence

John Maynard Keynes

Keynesian economics



John Maynard Keynes

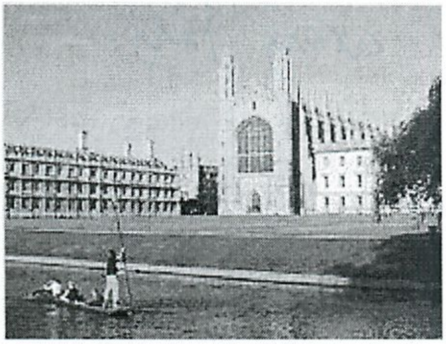
Born	5 June 1883 Cambridge, Cambridgeshire, England, United Kingdom
Died	21 April 1946 (aged 62) Tilton, near Firle, East Sussex, England, United Kingdom
Nationality	British
Field	Political economy, probability
Alma mater	King's College, Cambridge
Opposed	Marx · Hayek · Marshall · Pigou
Influences	Adam Smith · David Ricardo · David Hume · John Stuart Mill · Thomas Malthus · Silvio Gesell · G. E. Moore · Alfred Marshall · Knut Wicksell · Dennis Robertson · Michal Kalecki
Influenced	Simon Kuznets · Paul Samuelson · John Hicks · G. L. S. Shackle · William Vickrey · John Kenneth Galbraith · Hyman Minsky · Robert Shiller · Joseph Stiglitz · Paul Krugman · Joan Robinson · Stephany

	Griffith-Jones · Inge Kaul
Contributions	Macroeconomics, Keynesian economics, Liquidity preference, Spending multiplier, Aggregate Demand-Aggregate Supply model

In 1999, *Time* magazine included Keynes in their list of the 100 most important and influential people of the 20th century, commenting that: "His radical idea that governments should spend money they don't have may have saved capitalism."[8] In addition to being an economist, Keynes was also a civil servant, a director of the British Eugenics Society, a director of the Bank of England, a patron of the arts and an art collector, a part of the Bloomsbury Group of intellectuals,[9][10] an advisor to several charitable trusts, a writer, a philosopher, a private investor, and a farmer.

Contents

Early life and education



King's College, Cambridge. Keynes's grandmother wrote to him saying that since he was born in Cambridge, people will expect him to be clever.

John Maynard Keynes was born in Cambridge, Cambridgeshire, England, to an upper-middle-class family. His father John Neville Keynes was an economist and a lecturer in moral sciences at the University of Cambridge and his mother Florence Ada Keynes a local social reformer. Keynes was the first born, and was followed by two more children – Margaret Neville Keynes in 1885 and Geoffrey Keynes in 1887.

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According to the economist and biographer Robert Skidelsky, Keynes's parents were loving and attentive. They remained in the same house throughout their lives, where the children were always welcome to return. Keynes would receive considerable support from his father, including expert coaching to help him pass his scholarship exams and financial help both as a young man and when his assets were nearly wiped out at the onset of Great Depression in 1929. Keynes's mother made her children's interests her own, and according to Skidelsky, "because she could grow up with her children, they never outgrew home".[11]

Keynes had his early education at home and at nursery. He attended The Perse School nursery in 1890 before becoming a day pupil at St Faith's preparatory school in 1892.[12] Teachers described Keynes as brilliant, but on occasion, careless and lacking in determination. His health was often poor during this period, leading to several long absences.

Keynes won a scholarship to Eton College in 1897, where he displayed talent in a wide range of subjects, particularly mathematics, classics and history. At Eton, Keynes experienced the first "love of his life" in Dan Macmillan, older brother of the future Prime Minister Harold Macmillan.[13] Despite his middle-class background, Keynes mixed easily with upper-class pupils. In 1902 Keynes left Eton for King's College, Cambridge after receiving a scholarship for this also to study mathematics. Alfred Marshall begged Keynes to become an economist,[14] although Keynes's own inclinations drew him towards philosophy – especially the ethical system of G. E. Moore. Keynes was an active member of the semi-secretive Cambridge Apostles society, a debating club largely reserved for the brightest students. Like many members, Keynes retained a bond to the club after graduating and continued to attend occasional meetings throughout his life. Before leaving Cambridge, Keynes became the President of the Cambridge Union Society and Cambridge University Liberal Club. In May 1904 he received a first class B.A. in mathematics. Aside from a few months spent on holidays with family and friends, Keynes continued to involve himself with the university over the next two years. He took part in debates, further studied philosophy and attended economics lectures informally as a graduate student. He also studied for his 1905 Tripos and 1906 civil service exams.

The economist Harry Johnson wrote that the optimism imparted by Keynes's early life is key to understanding his later thinking.[15] Keynes was always confident he could find a solution to whatever problem he turned his attention to, and retained a lasting faith in the ability of government officials to do good.[16] Keynes's optimism was also cultural, in two sense – he was of the last generation raised by an empire still at the height of its power, in its own eyes and by much of the world (at least outwardly) seen as preeminent in both power and benevolence. Keynes was also of the last generation who felt entitled to govern by culture, rather than by expertise. According to Skidelsky, the sense of cultural unity current in Britain from the 19th century to the end of World War I provided a framework with which the well-educated could set various spheres of knowledge in relation to each other and to life, enabling them to confidently draw from different fields when addressing practical problems.[11]

Career

Printed the wrong thing...

Keynes's Civil Service career began in October 1906, as a clerk in the India Office. He enjoyed his work at first, but by 1908 had become bored and resigned his position to return to Cambridge and work on probability theory, at first privately funded only by two dons at the university – his father and the economist Arthur Pigou. In 1909 Keynes published his first professional economics article in the *Economics Journal*, about the effect of a recent global economic downturn on India.[17] Also in 1909, Keynes accepted a lectureship in economics funded personally by Alfred Marshall. Keynes's earnings rose further as he began to take on pupils for private tuition, and on being elected a fellow. In 1911 Keynes was made editor of *The Economic Journal*. By 1913 he had published his first book, *Indian Currency and Finance*. He was then appointed to the Royal Commission on Indian Currency and Finance[18] – the same topic as his book – where Keynes showed considerable talent at applying economic theory to practical problems.

World War I

The British Government called on Keynes's expertise during the First World War. While he did not formally re-join the civil service in 1914, Keynes travelled to London at the government's request a few days before hostilities started. Bankers had been pushing for the suspension of specie payments – the convertibility of banknotes into gold – but with Keynes's help the Chancellor of the Exchequer (then Lloyd George) was persuaded that this would be a bad idea, as it would hurt the future reputation of the city if payments were suspended before absolutely necessary.

In January 1915 Keynes took up an official government position at the Treasury. Among his responsibilities were the design of terms of credit between Britain and its continental allies during the war, and the acquisition of scarce currencies. According to economist Robert Lekachman, Keynes's "nerve and mastery became legendary" because of his performance of these duties, as in the case where he managed to assemble – with difficulty – a small supply of Spanish pesetas. The secretary of the Treasury was delighted to hear Keynes had amassed enough to provide a temporary solution for the British Government. But Keynes did not hand the pesetas over, choosing instead to sell them all to break the market: his boldness paid off, as pesetas then became much less scarce and expensive.[19] In the 1917 King's Birthday Honours, Keynes was appointed Companion of the Order of the Bath for his wartime work,[20] and his success led to the appointment that would have a huge effect on Keynes's life and career; Keynes was appointed financial representative for the Treasury to the 1919 Versailles peace conference. He was also appointed Officer of the Belgian Order of Leopold.[21]

Versailles peace conference

Main article: Heavenly Twins (Sumner and Cunliffe)

Keynes's colleague, David Lloyd George. Keynes was initially wary of the "Welsh Wizard," preferring his rival Asquith, but was impressed with Lloyd George at Versailles; this did not prevent Keynes from painting a scathing picture of the then-Prime Minister in his *Economic Consequences of the Peace*.

Keynes's experience at Versailles was influential in shaping his future outlook, yet it was not a successful one for him. Keynes's main interest had been in trying to prevent Germany's compensation payments being set so high it would traumatise innocent German people, damage the nation's ability to pay and sharply limit her ability to buy exports from other countries – thus hurting not just Germany's own economy but that of the wider world. Unfortunately for Keynes, conservative powers in the coalition that emerged from the 1918 coupon election were able to ensure that both Keynes himself and the Treasury were largely excluded from formal high-level talks concerning reparations. Their place was taken by the Heavenly Twins – the judge Lord Sumner and the banker Lord Cunliffe whose nickname derived from the "astronomically" high war compensation they wanted to demand from Germany. Keynes was forced to try to exert influence mostly from behind the scenes.

The three principal players at Versailles were Britain's Lloyd George, France's Clemenceau and America's President Wilson.[22] It was only Lloyd George to whom Keynes had much direct access; until the 1918 election he had some sympathy with Keynes's view but while campaigning had found his speeches were only well received by the public if he promised to harshly punish Germany, and had therefore committed to extracting high payments. Lloyd George did however win some loyalty from Keynes with his actions at the Paris conference by intervening against the French to ensure the dispatch of much-needed food supplies to German civilians. Clemenceau also pushed for high reparations; generally France argued for an even more severe settlement than Britain. Wilson initially favoured relatively lenient treatment of Germany – he feared too harsh conditions could foment the rise of extremism, and wanted Germany to be left sufficient capital to pay for imports. To Keynes's dismay, Lloyd George and Clemenceau were able to pressure Wilson to agree to very high repayments being imposed. Towards the end of the conference, Keynes came up with a plan that he argued would not only help Germany and other impoverished central European powers but also be good for the world economy as a whole. It involved the writing down of war debts which would have the effect of increasing international trade all round. Lloyd George agreed it might be acceptable to the British electorate. However, America was against it; the US was then the largest creditor and by this time Wilson had started to believe in the merits of a harsh peace as a warning to future aggressors. Hence despite his best efforts, the end result of the conference was a treaty which disgusted Keynes both on moral and economic grounds, and led to his resignation from the Treasury.[23]

In June 1919 he turned down an offer to become chairman of the British Bank of Northern Commerce, a job that promised a salary of £2000 in return for a morning per week of work.

Keynes's analysis on the predicted damaging effects of the treaty appeared in the highly influential book, *The Economic Consequences of the Peace*, published in 1919.[24] This work has been described as Keynes's best book, where he was able to bring all his gifts to bear – his passion as well as his skill as an economist. In addition to economic analysis, the book contained pleas to the reader's sense of compassion:

> I cannot leave this subject as though its just treatment wholly depended either on our own pledges or on economic facts. The policy of reducing Germany to servitude for a generation, of degrading the lives of millions of human beings, and of depriving a whole nation of happiness should be abhorrent and detestable,--abhorrent and detestable, even if it were possible, even if it enriched ourselves, even if it did not sow the decay of the whole civilised life of Europe.

Also present was striking imagery such as "...that year by year Germany must be kept impoverished and her children starved and crippled..." along with bold predictions which were later justified by events:

> If we aim deliberately at the impoverishment of Central Europe, vengeance, I dare predict, will not limp. Nothing can then delay for very long that final war between the forces of Reaction and the despairing convulsions of Revolution, before which the horrors of the late German war will fade into nothing.

Keynes's predictions of disaster were borne out when the German economy suffered the hyperinflation of 1923, and again by the collapse of the Weimar Republic and the outbreak of World War II. Only a fraction of reparations were ever paid. *The Economic Consequences of the Peace* gained Keynes international fame, but also caused him to be regarded as anti-establishment – it was not until after the outbreak of World War II that Keynes was offered a directorship of a major British Bank, or an acceptable offer to return to government with a formal job. However, Keynes was still able to influence government policy making through his network of contacts, his published works and by serving on government committees; this included attending high-level policy meetings as a consultant.[23]

In the 1920s

Keynes argued against a return to the gold standard after the war.

Keynes had completed his *A Treatise on Probability* before the war, but published it in 1921.[23] The work was a notable contribution to the philosophical and mathematical underpinnings of probability theory, championing the important view that *probabilities* were no more or less than truth values intermediate between simple truth and falsity. Keynes developed the first upper-lower probabilistic interval approach to probability in chapters 15 and 17 of this book, as well as having developed the first decision weight approach with his conventional coefficient of risk and weight, *c*, in chapter 26. In addition to his academic work, the 1920s saw Keynes active as a journalist selling his work internationally and working in London as a financial consultant. In 1924 Keynes wrote an obituary for his former tutor Alfred Marshall which Schumpeter called "the most brilliant life of a man of science I have ever read."[25] Marshall's widow was "entranced" by the memorial, while Lytton Strachey rated it as one of Keynes's "best works".[23]

In 1922 Keynes continued to advocate reduction of German reparations with *A Revision of the Treaty*.[23] He attacked the post World War I deflation policies with *A Tract on Monetary Reform* in 1923[23] – a trenchant argument that countries should target stability of domestic prices, avoiding deflation even at the cost of allowing their currency to depreciate. Britain suffered from high unemployment through most of the 1920s, leading Keynes to recommend the depreciation of sterling to boost jobs by making British exports more affordable. From 1924 he was also advocating a fiscal response, where the government could create jobs by spending on public works.[23] During the 1920s Keynes's pro stimulus views had only limited effect on policy makers and mainstream academic opinion – according to Hyman Minsky one reason was that at this time his theoretical justification was "muddled" .[17] The *Tract* had also called for an end to the gold standard. Keynes advised it was no longer a net benefit for countries such as Britain to participate in the gold standard, as it ran counter to the need for domestic policy autonomy. It could force countries to pursue deflationary policies at exactly the time when expansionary measures were called for to address rising unemployment. The Treasury and Bank of England were still in favour of the gold standard and in 1925 they were able to convince the then Chancellor Winston Churchill to re-establish it, which had a depressing effect on British industry. Keynes responded by writing *The Economic Consequences of Mr. Churchill* and continued to argue against the gold standard until Britain finally abandoned it in 1931.[23]

During the Great Depression

Keynes had begun a theoretical work to examine the relationship between unemployment, money and prices back in the 1920s.[26] The work, *Treatise on Money*, was published in 1930 in two volumes. A central idea of the work was that if the amount of money being saved exceeds the amount being invested – which can happen if interest rates are too high – then unemployment will rise. This is in part a result of people not wanting to spend too high a proportion of what employers pay out, making it difficult, in aggregate, for employers to make a profit.

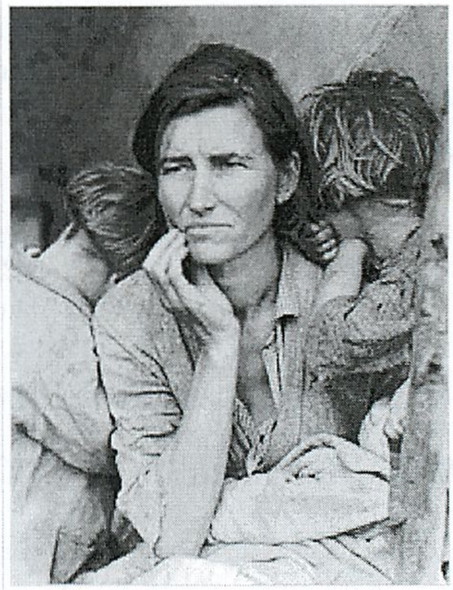
Keynes was deeply critical of the British government's austerity measures during the Great Depression. He believed that budget deficits were a good thing, a product of recessions. He wrote, "For Government borrowing of one kind or another is nature's remedy, so to speak, for preventing business losses from being, in so severe a slump as to present one, so great as to bring production altogether to a standstill."[27]

At the height of the Great Depression, in 1933, Keynes published *The Means to Prosperity*, which contained specific policy recommendations for tackling unemployment in a global recession, chiefly counter cyclical public spending. *The Means to Prosperity* contains one of the first mentions of the multiplier effect. While it was addressed chiefly to the British Government, it also contained advice for other nations affected by the global recession. A copy was sent to the newly elected President Roosevelt and other world leaders. The work was taken seriously by both the American and British governments, and according to Skidelsky, helped pave the way for the later acceptance of Keynesian ideas, though it had little immediate practical influence. In the 1933 London Economic Conference opinions remained too diverse for a unified course of action to be agreed upon.[28]

Keynesian-like policies were adopted by Sweden and Germany, but Sweden was seen as too small to command much attention, and Keynes was deliberately silent about the successful efforts of Germany as he was dismayed by their imperialist ambitions and their treatment of Jews.[28] Apart from Great Britain, Keynes's attention was primarily focused on the United States. In 1931, he received considerable support for his views on counter-cyclical public spending in Chicago, then America's foremost centre for economic views alternative to the mainstream.[17][28] However, orthodox economic opinion remained generally hostile regarding fiscal intervention to mitigate the depression, until just before the outbreak of war.[17] In late 1933 Keynes was persuaded by Felix Frankfurter to address President Roosevelt directly, which he did by letters and face to face in 1934, after which the two men spoke highly of each other.[28] However according to Skidelsky, the consensus is that Keynes's efforts only began to have a more than marginal influence on US economic policy after 1939.[28]

Keynes's *magnum opus*, *The General Theory of Employment, Interest and Money* was published in 1936. It was researched and indexed by one of Keynes's favourite students, later the economist David Bensusan-Butt.[29] The work served as a theoretical justification for the interventionist policies Keynes favoured for tackling a recession. The *General Theory* challenged the earlier neo-classical economic paradigm, which had held that provided it was unfettered by government interference, the market would naturally establish full employment equilibrium. In doing so Keynes was partly setting himself against his former teachers Marshall and Pigou. Keynes believed the classical theory was a "special case" that applied only to the particular conditions present in the 19th century, his own theory being the general one. Classical economists had believed in Say's law, which, simply put, states that "supply creates its own demand", and that in a free market workers would always be willing to lower their wages to a level where employers could profitably offer them jobs. An innovation from Keynes was the concept of price stickiness – the recognition that in reality workers often refuse to lower their wage demands even in cases where a classical economist might argue it is rational for them to do so. Due in part to price stickiness, it was established that the interaction of "aggregate demand" and "aggregate supply" may lead to stable unemployment equilibria – and in those cases, it is the state, and not the market, that economies must depend on for their salvation.

his was more relevant



The Great Depression with its periods of world wide economic hardship formed the backdrop against which Keynes's revolution took place. The image is Dorothea Lange's *Migrant Mother* depiction of destitute pea-pickers in California, taken in March 1936.

The *General Theory* argues that demand, not supply, is the key variable governing the overall level of economic activity. Aggregate demand, which equals total un-hoarded income in a society, is defined by the sum of consumption and investment. In a state of unemployment and unused production capacity, one can *only* enhance employment and total income by *first* increasing expenditures for either consumption or investment. Without government intervention to increase expenditure, an economy can remain trapped in a low employment equilibrium – the demonstration of this possibility has been described as the revolutionary formal achievement of the work.[30] The book advocated activist economic policy by government to stimulate demand in times of high unemployment, for example by spending on public works. "Let us be up and doing, using our idle resources to increase our wealth," he wrote in 1928. "With men and plants unemployed, it is ridiculous to say that we cannot afford these new developments. It is precisely with these plants and these men that we shall afford them."[27]

The *General Theory* is often viewed as the foundation of modern macroeconomics. Few senior American economists agreed with Keynes through most of the 1930s.[31] Yet his ideas were soon to achieve widespread acceptance, with eminent American professors such as Alvin Hansen agreeing with the *General Theory* before the outbreak of World War II.[32][33] [34]

Keynes himself had only limited participation in the theoretical debates that followed the publication of the *General Theory* as he suffered a heart attack in 1937, requiring him to take long periods of rest. Hyman Minsky and other post-Keynesian economists have argued that as result of this, Keynes's ideas were diluted by those keen to compromise with classical economists or to render his concepts with mathematical models like the IS/LM model (which, they argue, distort Keynes's ideas).[17][34] Keynes began to recover in 1939, but for the rest of his life his professional energies were largely directed towards the practical side of economics – the problems of ensuring optimum allocation of resources for the War efforts, post-War negotiations with America, and the new international financial order that was presented at Bretton Woods, New Hampshire.

World War II

During World War II, Keynes argued in *How to Pay for the War*, published in 1940, that the war effort should be largely financed by higher taxation and especially by compulsory saving (essentially workers lending money to the government), rather than deficit spending, in order to avoid inflation. Compulsory saving would act to dampen domestic demand, assist in channelling additional output towards the war efforts, would be fairer than punitive taxation and would have the advantage of helping to avoid a post war slump by boosting demand once workers were allowed to withdraw their savings. In September 1941 he was proposed to fill a vacancy in the Court of Directors of the Bank of England, and subsequently carried out a full term from the following April.[35] In June 1942, Keynes was rewarded for his service with a hereditary peerage in the King's Birthday Honours.[36] On 7 July his title was gazetted as "BARON KEYNES, of Tilton, in the County of Sussex" and he took his seat in the House of Lords on the Liberal Party benches.[37]

Keynes (right) and the US representative Harry Dexter White at the Bretton Woods Conference in 1944.

As the Allied victory began to look certain, Keynes was heavily involved, as leader of the British delegation and chairman of the World Bank commission, in the mid-1944 negotiations that established the Bretton Woods system. The Keynes-plan, concerning an international clearing-union argued for a radical system for the management of currencies. He proposed the creation of a common world unit of currency, the bancor, and new global institutions – a world central bank and the International Clearing Union. Keynes envisaged these institutions managing an international trade and payments system with strong incentives for countries to avoid substantial trade deficits or surpluses. The USA's greater negotiating strength, however, meant that the final outcomes accorded more closely to the more conservative plans of Harry Dexter White. According to US economist Brad Delong, on almost every point where he was overruled by the Americans, Keynes was later proved correct by events.[38]

The two new institutions, later known as the World Bank and International Monetary Fund (IMF), were founded as a compromise that primarily reflected the American vision. There would be no incentives for states to avoid a large trade surplus; instead, the burden for correcting a trade imbalance would continue to fall only on the deficit countries, which Keynes had argued were least able to address the problem without inflicting economic hardship on their populations. Yet, Keynes was still pleased when accepting the final agreement, saying that if the institutions stayed true to their founding principles, "the brotherhood of man will have become more than a phrase."[39][40]

Postwar

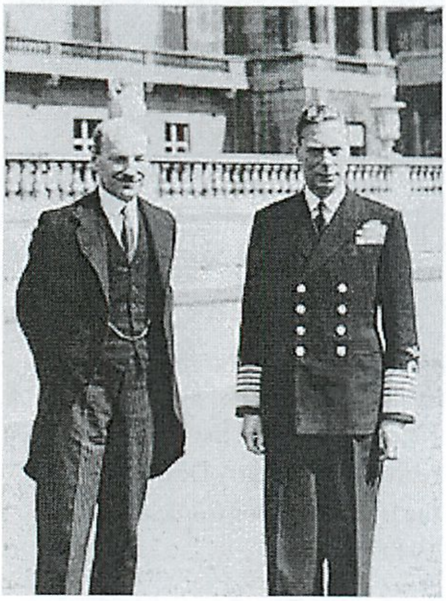
After the war, Keynes continued to represent the United Kingdom in international negotiations despite his deteriorating health. He succeeded in obtaining preferential terms from the United States for new and outstanding debts to facilitate the rebuilding of the British economy.[41]

Just before his death in 1946, Keynes told Henry Clay, a professor of Social Economics and Advisor to the Bank of England [42] of his hopes that Adam Smith's 'invisible hand' can help Britain out of the economic hole it is in: "I find myself more and more relying for a solution of our problems on the invisible hand which I tried to eject from economic thinking twenty years ago." [43]

Legacy

The Keynesian ascendancy 1939–1979

Main article: Keynesian Revolution



Prime Minister Clement Attlee with King George VI after his 1945 election victory.

From the end of the Great Depression to the mid-1970s, Keynes provided the main inspiration for economic policy makers in Europe, America and much of the rest of the world.[34] While economists and policy makers had become increasingly won over to Keynes's way of thinking in the mid and late 1930s, it was only after the outbreak of World War II that governments started to borrow money for spending on a scale sufficient to eliminate unemployment. According to economist John Kenneth Galbraith (then a US government official charged with controlling inflation), in the rebound of the economy from wartime spending, "one could not have had a better demonstration of the Keynesian ideas."[44]

The Keynesian Revolution was associated with the rise of modern liberalism in the West during the post-war period.[45] Keynesian ideas became so popular that some scholars point to Keynes as representing the ideals of modern liberalism, as Adam Smith represented the ideals of classical liberalism.[46] After the war Winston Churchill attempted to check the rise of Keynesian policy-making in the United Kingdom, and used rhetoric critical of the mixed economy in his 1945 election campaign. Despite his popularity as a war hero Churchill suffered a landslide defeat to Clement Attlee whose government's economic policy continued to be influenced by Keynes's ideas.[44]

Neo-Keynesian economics

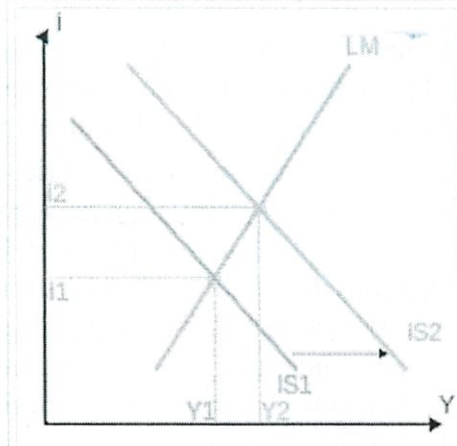
Main article: Neo-Keynesian economics

WP: IS/LM
Phillips Curve ↓ unemp = ↑ inflation

In the late 1930s and 1940s, economists (notably John Hicks, Franco Modigliani, and Paul Samuelson) attempted to interpret and formalise Keynes's writings in terms of formal mathematical models. In a process termed "the neoclassical synthesis", they combined Keynesian analysis with neo-classical economics to produce Neo-Keynesian economics, which came to dominate mainstream macroeconomic thought for the next 40 years.

how were they diff?

By the 1950s, Keynesian policies were adopted by almost the entire developed world and similar measures for a mixed economy were used by many developing nations. By then, Keynes's views on the economy had become mainstream in the world's universities. Throughout the 1950s and 1960s, the developed and emerging free capitalist economies enjoyed exceptionally high growth and low unemployment.[47] [48] Professor Gordon Fletcher has written that the 1950s and 1960s, when Keynes's influence was at its peak, appear in retrospect as a Golden Age of Capitalism.[34]



The *IS/LM model* is used to analyse the effect of demand shocks on the economy.

In late 1965 *Time* magazine ran a cover article with the title inspired by a possibly tongue-in-cheek comment from Milton Friedman, a comment later echoed by U.S. President Richard Nixon, that "We are all Keynesians now". The article described the exceptionally favourable economic conditions then prevailing, and reported that "Washington's economic managers scaled these heights by their adherence to Keynes's central theme: the modern capitalist economy does not automatically work at top efficiency, but can be raised to that level by the intervention and influence of the government." The article also states that Keynes was one of the three most important economists who ever lived, and that his *General Theory* was more influential than the *magna opera* of other famous economists, like Smith's *The Wealth of Nations*.[49]

people followed it

Economics: out of favour 1979–2007

Main article: Post-war displacement of Keynesianism

Keynesian economics were officially discarded by the British Government in 1979, but forces had begun to gather against Keynes's ideas over 30 years earlier. Friedrich Hayek had formed the Mont Pelerin Society in 1947, with the explicit intention of nurturing intellectual currents to one day displace Keynesianism and other similar influences. Its members included Austrian School economist Ludwig von Mises along with the then young Milton Friedman. Initially the society had little impact on the wider world – Hayek was to say it was as if Keynes had been raised to sainthood after his death and that people refused to allow his work to be questioned.[50][51] Friedman however began to emerge as a formidable critic of Keynesian economics from the mid-1950s, and especially after his 1963 publication of *A Monetary History of the United States*.

wish had more time to read

On the practical side of economic life, big government had appeared to be firmly entrenched in the 1950s but the balance began to shift towards private power in the 1960s. Keynes had written against the folly of allowing "decadent and selfish" speculators and financiers the kind of influence they had enjoyed after World War I. For two decades after World War II public opinion was strongly against private speculators, the disparaging label Gnomes of Zürich being typical of how they were described during this period. International speculation was severely restricted by the capital controls in place after Bretton Woods. Journalists Larry Elliott and Dan Atkinson say 1968 was a pivotal year when power shifted in the favour of private agents such as currency speculators. They pick out a key 1968 event as being when America suspended the conversion of the dollar into gold except on request of foreign governments, which they identify as when the Bretton Woods system first began to break down. [52]

Criticisms of Keynes's ideas had begun to gain significant acceptance by the early 1970s as they were able to make a credible case that Keynesian models no longer reflected economic reality. Keynes himself had included few formulæ and no explicit mathematical models in his General Theory. For commentators such as economist Hyman Minsky, Keynes's limited use of mathematics was partly the result of his scepticism about whether phenomena as inherently uncertain as economic activity could ever be adequately captured by mathematical models. Nevertheless, many models were developed by Keynesian economists, with a famous example being the Phillips curve which predicted an inverse relationship between unemployment and inflation. It implied that unemployment could be reduced by government stimulus with a calculable cost to inflation. In 1968 Milton Friedman published a paper arguing that the fixed relationship implied by the Philips curve did not exist.[53] Friedman suggested that sustained Keynesian policies could lead to both unemployment and inflation rising at once – a phenomenon that soon became known as stagflation. In the early 1970s stagflation appeared in both the US and Britain just as Friedman had predicted, with economic conditions deteriorating further after the 1973 oil crisis. Aided by the prestige gained from his successful forecast, Friedman led increasingly successful criticisms against the Keynesian consensus, convincing not only academics and politicians but also much of the general public with his radio and television broadcasts. The academic credibility of Keynesian economics was further undermined by additional criticism from other Monetarists trained in the Chicago school of economics, by the Lucas Critique and by criticisms from Hayek's Austrian School.[34] So successful were these criticisms that by 1980 Robert Lucas was saying economists would often take offence if described as Keynesians.[54] Keynesian principles fared increasingly poorly on the practical side of economics – by 1979 they had been displaced by Monetarism as the primary influence on Anglo-American economic policy.[34] However many officials on both sides of the Atlantic retained a preference for Keynes, and in 1984 the Federal Reserve officially discarded monetarism, after which Keynesian principles made a partial comeback as an influence on policy making.[55] Not all academics accepted the criticism against Keynes – Minsky has argued that Keynesian economics had been debased by excessive mixing with neo-classical ideas from the 1950s, and that it was unfortunate the branch of economics had even continued to be called "Keynesian".[17] Writing in *The American Prospect* Robert Kuttner argued it was not so much excessive Keynesian activism that caused the economic problems of the 1970s but the breakdown of the Bretton Woods system of capital controls, which allowed capital flight from regulated economies into unregulated economies in a fashion similar to Gresham's Law (where weak currencies undermine strong currencies).[56] Historian Peter Pugh has stated a key cause of the economic problems afflicting America in the 1970s was the refusal to raise taxes to finance the Vietnam War, which was against Keynesian advice.[57]

What caused it? external shock?

how does this work?

A more typical response was to accept some elements of the criticisms while refining Keynesian economic theories to defend them against arguments that would invalidate the whole Keynesian framework – the resulting body of work largely composing New Keynesian economics. In 1992 Alan Blinder was writing about a "Keynesian Restoration" as work based on Keynes's ideas had to some extent become fashionable once again in academia, though in the mainstream it was highly synthesised with Monetarism and other neo-classical thinking. In the world of policy making, free-market influences broadly sympathetic to Monetarism remained very strong at government level – in powerful normative institutions like the World Bank, IMF and US Treasury, and in prominent opinion-forming media such as the *Financial Times* and *The Economist*.[58]

Economics: the Keynesian resurgence of 2008–2009

Main article: 2008–2009 Keynesian resurgence

The 2007–2012 global financial crisis led to public skepticism about the free market consensus even from some on the economic right. In March 2008, Martin Wolf, chief economics commentator at the *Financial Times*, announced the death of the dream of global free-market capitalism.[59] In the same month macroeconomist James K. Galbraith used the 25th Annual Milton Friedman Distinguished Lecture to launch a sweeping attack against the consensus for monetarist economics and argued that Keynesian economics

Wage controls amt of it — Friedman

were far more relevant for tackling the emerging crises.[60] Economist Robert Shiller had begun advocating robust government intervention to tackle the financial crises, specifically citing Keynes.[61][62][63] Nobel laureate Paul Krugman also actively argued the case for vigorous Keynesian intervention in the economy in his columns for the *New York Times*.[64][65][66] Other prominent economic commentators arguing for Keynesian government intervention to mitigate the financial crisis include George Akerlof,[67] Brad Delong,[68] Robert Reich,[69] and Joseph Stiglitz.[70][71] Newspapers and other media have also cited work relating to Keynes by Hyman Minsky,[17] Robert Skidelsky,[11] Donald Markwell[72] and Axel Leijonhufvud.[73]

Economist and current prime Minister of India Manmohan Singh spoke in favour of Keynesian fiscal stimuli at the 2008 G-20 Washington summit

A series of major bail-outs were pursued during the financial crisis, starting on 7 September with the announcement that the U.S. government was to nationalise the two government-sponsored enterprises which oversaw most of the U.S. subprime mortgage market – Fannie Mae and Freddie Mac. In October, the British Chancellor of the Exchequer referred to Keynes as he announced plans for substantial fiscal stimulus to head off the worst effects of recession, in accordance with Keynesian economic thought.[74][75] Similar policies have been adopted by other governments worldwide.[76][77] This is in stark contrast to the action permitted to Indonesia during its financial crisis of 1997, when it was forced by the IMF to close 16 banks at the same time, prompting a bank run.[78] Much of the recent discussion reflected Keynes's advocacy of international coordination of fiscal or monetary stimulus, and of international economic institutions such as the IMF and the World Bank, which many had argued should be reformed at a "new Bretton Woods", even before the crises broke out.[79] IMF and United Nations economists advocated a coordinated international approach to fiscal stimulus.[80] Donald Markwel argued that in the absence of such an international approach, there would be a risk of worsening international relations and possibly even world war arising from similar economic factors to those present during the depression of the 1930s.[72]

I don't get Bretton Woods

By the end of December 2008, the *Financial Times* reported that "the sudden resurgence of Keynesian policy is a stunning reversal of the orthodoxy of the past several decades."[81] In December 2008, Paul Krugman released his book, *The Return of Depression Economics and the Crisis of 2008*, arguing that economic conditions similar to what existed during the earlier part of the 20th century had returned, making Keynesian policy prescriptions more relevant than ever. In February 2009 Shiller and George Akerlof published *Animal Spirits*, a book where they argue the current US stimulus package is too small as it does not take into account Keynes's insight on the importance of confidence and expectations in determining the future behaviour of businessmen and other economic agents.

In a March 2009 speech entitled *Reform the International Monetary System*, Zhou Xiaochuan, the governor of the People's Bank of China came out in favour of Keynes's idea of a centrally managed global reserve currency. Zhou argued that it was unfortunate that part of the reason for the Bretton Woods system breaking down was the failure to adopt Keynes's bancor. Zhou proposed a gradual move towards increased use of IMF special drawing rights (SDRs).[82][83] Although Zhou's ideas have not yet been broadly accepted, leaders meeting in April at the 2009 G-20 London summit agreed to allow $250 billion of special drawing rights to be created by the IMF, to be distributed globally. Stimulus plans have been credited for contributing

How do those polices get approved in China?

to a better than expected economic outlook by both the OECD[84] and the IMF,[85][86] in reports published in June and July 2009. Both organisations warned global leaders that recovery is likely to be slow, so counter recessionary measures ought not be rolled back too early.

While the need for stimulus measures has been broadly accepted among policy makers, there has been much debate over how to fund the spending. Some leaders and institutions such as Angela Merkel[87] and the European Central Bank[88] have expressed concern over the potential impact on inflation, national debt and the risk that a too large stimulus will create an unsustainable recovery.

Among professional economists the revival of Keynesian economics has been even more divisive. Although many economists, such as George Akerlof, Paul Krugman, Robert Shiller, and Joseph Stiglitz, support Keynesian stimulus, over 300 economists signed a petition stating that they do not believe higher government spending will help the United States economy recover from the late-2000s recession. Some economists, such as Robert Lucas, questioned the theoretical basis for stimulus packages.[89] Others, like Robert Barro and Gary Becker, say that the empirical evidence for beneficial effects from Keynesian stimulus does not exist.[90] However, there is a growing academic literature that shows that fiscal expansion helps an economy grow in the near term, and that certain types of fiscal stimulus are particularly effective.[91][92]

Reception

Praise

Keynes's economic thinking only began to achieve close to universal acceptance in the last few years of his life. On a personal level, Keynes's charm was such that he was generally well received wherever he went – even those who found themselves on the wrong side of his occasionally sharp tongue rarely bore a grudge.[93] Keynes's speech at the closing of the Bretton Woods negotiations was received with a lasting standing ovation, rare in international relations, as delegates acknowledged the scale of his achievements made despite poor health.[16]

Hayek

Austrian School economist Friedrich Hayek was Keynes's most prominent contemporary critic, with sharply opposing views on the economy.[30] Yet after Keynes's death he wrote:[94]

> He was the one really great man I ever knew, and for whom I had unbounded admiration. The world will be a very much poorer place without him.

For his part, Keynes praised Hayek's book *The Road to Serfdom*, writing to the Austrian economist that, "Morally and philosophically I find myself in agreement with virtually the whole of it."[27]

Lionel Robbins

Lionel Robbins, former head of the economics department at the London School of Economics, who had many heated debates with Keynes in the 1930s, had this to say after observing Keynes in early negotiations with the Americans while drawing up plans for Bretton Woods:[30]

> This went very well indeed. Keynes was in his most lucid and persuasive mood: and the effect was irresistible. At such moments, I often find myself thinking that Keynes must be one of the most remarkable men that have ever lived – the quick logic, the birdlike swoop of intuition, the vivid fancy, the wide vision, above all the incomparable sense of the fitness of words, all combine to make something several degrees beyond the limit of ordinary human achievement.

LePan

Douglas LePan,[30] an official from the Canadian High Commission, wrote:

> I am spellbound. This is the most beautiful creature I have ever listened to. Does he belong to our species? Or is he from some other order? There is something mythic and fabulous about him. I sense in him something massive and sphinx like, and yet also a hint of wings.

Russell

Bertrand Russell[95] named Keynes one of the most intelligent people he had ever known, commenting:

> Every time I argued with Keynes, I felt that I took my life in my hands and I seldom emerged without feeling something of a fool.

The Times

Keynes's obituary in *The Times* included the comment:[32]

> There is the man himself – radiant, brilliant, effervescent, gay, full of impish jokes ... He was a humane man genuinely devoted to the cause of the common good.

Critiques

As a man of the centre described as undoubtedly having the greatest impact of any 20th-century economist,[26] Keynes attracted considerable criticism from both sides of the political spectrum. In the 1920s, Keynes was seen as anti-establishment and was mainly attacked from the right. In the "red 1930s", many young economists favoured Marxist views, even in Cambridge,[17] and while Keynes was engaging principally with the right to try to persuade them of the merits of more progressive policy, the most vociferous criticism against him came from the left, who saw him as a supporter of capitalism. From the 1950s and onwards, most of the attacks against Keynes have again been from the right.

Hayek

In 1931 Friedrich Hayek extensively critiqued Keynes's 1930 *Treatise on Money*.[96] After reading Hayek's *The Road to Serfdom*, Keynes[97] wrote to Hayek saying: "Morally and philosophically I find myself in agreement with virtually the whole of it" but concluded the same letter with the recommendation:

> What we need therefore, in my opinion, is not a change in our economic programmes, which would only lead in practice to disillusion with the results of your philosophy; but perhaps even the contrary, namely, an enlargement of them. Your greatest danger is the probable practical

> failure of the application of your philosophy in the United States.

Friedrich Hayek, one of Keynes's most prominent critics

On the pressing issue of the time, whether deficit spending could lift a country from depression, Keynes[98] replied to Hayek's criticism in the following way:

> I should... conclude rather differently. I should say that what we want is not no planning, or even less planning, indeed I should say we almost certainly want more. But the planning should take place in a community in which as many people as possible, both leaders and followers wholly share your own moral position. Moderate planning will be safe enough if those carrying it out are rightly oriented in their own minds and hearts to the moral issue.

Hayek explained the letter by saying:[99]

> Because Keynes believed that he was fundamentally still a classical English liberal and wasn't quite aware of how far he had moved away from it. His basic ideas were still those of individual freedom. He did not think systematically enough to see the conflicts.

Hayek felt that application of Keynes's policies would give too much power to the state and would lead to socialism.[100]

Friedman

While Milton Friedman described *The General Theory* as "a great book", he argues that its implicit separation of nominal from real magnitudes is neither possible nor desirable. Macroeconomic policy, Friedman argues, can reliably influence only the nominal.[101] He and other monetarists have consequently argued that Keynesian economics can result in stagflation, the combination of low growth and high inflation that developed economies suffered in the early 1970s. More to Friedman's taste was the *Tract on Monetary Reform* (1923), which he regarded as Keynes's best work because of its focus on maintaining domestic price stability.[101]

don't get that criticism

Schumpeter

Joseph Schumpeter was an economist of the same age as Keynes and one of his main rivals. He was among the first reviewers to argue that Keynes's *General Theory* was not a general theory, but was in fact a special case.[102] He said the work expressed "the attitude of a decaying civilisation" (lol). After Keynes's death Schumpeter wrote a brief biographical piece called *Keynes the Economist* – on a personal level he was very positive about Keynes as a man ; praising his pleasant nature, courtesy and kindness. He assessed some of Keynes biographical and editorial work as among the best he'd ever seen. Yet Schumpeter remained critical about Keynes's economics, linking Keynes's childlessness to what Schumpeter saw as an essentially short term view. He considered Keynes to have a kind of unconscious patriotism that caused him to fail to understand the problems of other nations. For Schumpeter[103] "Practical Keynesianism is a seedling which cannot be transplanted into foreign soil: it dies there and becomes poisonous as it dies."

Hazlitt

What exactly has wrong → guess have to do next time

Austrian School economic commentator and journalist Henry Hazlitt's *The Failure of the New Economics* is a paragraph-by-paragraph critique of *The General Theory*. In 1960 he published the book *The Critics of Keynesian Economics* where he gathered together the major criticisms of Keynes made up to that year.[31]

Harry Truman

President Harry Truman was skeptical of Keynesian theorizing. "Nobody can ever convince me that Government can spend a dollar that it's not got," he told Leon Keyserling, a Keynesian economist who chaired Truman's Council of Economic Advisers.[27]

lol

Allegations of racism

Keynes was on occasion heard making statements which could be perceived as racist: for example, he would use the word "niggers" to refer to black people in casual conversations.[104] This term was often used neutrally in British circles at that time, and was not necessarily an expression of negative feelings, as when, for example, he wrote to Duncan Grant that "the only really sympathetic and original thing in America are the niggers, who are charming".[105] Nonetheless fellow British observers recount being shocked by some statements he made, such as the following, apropos the Washington summer: "It's far too hot. Much too hot for white men. All right for niggers."[104] He also wrote that there was "beastliness in the Russian nature" as well as "cruelty and stupidity", and other comments which may be construed as anti-Russian.[106] Some critics, such as Rothbard, have sought to infer that Keynes had sympathy with Nazism, and a number of writers have described him as anti-Semitic. Keynes's private letters express portraits and descriptions some of which can be characterised as anti-Semitic, others as pro-Semitic.[107][108] Scholars have suggested that these reflect clichés current at the time that he accepted uncritically, rather than any racism.[105] Keynes had many Jewish friends, including Isaiah Berlin and Piero Sraffa.[109][110] Keynes several times used his influence to help his Jewish friends, most notably when he successfully lobbied for Ludwig Wittgenstein to be allowed residency in the United Kingdom explicitly in order to rescue him from being deported to Nazi-occupied Austria. Keynes was, furthermore, a supporter of Zionism, serving on committees supporting the cause.[105]

Common at the time — not appropriate now

Allegations that he was racist or had totalitarian beliefs have been rejected by biographers such as Robert Skidelsky.[16] Professor Gordon Fletcher writes that "the suggestion of a link between Keynes and any support of totalitarianism cannot be sustained".[34] Once the aggressive tendencies of the Nazis towards Jews and other minorities became apparent, Keynes made clear his loathing of Nazism. As a lifelong pacifist he had initially favoured peaceful containment, yet he began to advocate a forceful resolution while many conservatives were still arguing for appeasement. After the war started he roundly criticised the Left for losing their nerve to confront Hitler.[30]

> The intelligentsia of the Left were the loudest in demanding that the Nazi aggression should be resisted at all costs. When it comes to a showdown, scarce four weeks have passed before they remember that they are pacifists and write defeatist letters to your columns, leaving the defence of freedom and civilisation to Colonel Blimp and the Old School Tie, for whom Three Cheers.

Allegations of pro-inflationary views

Keynes has been characterised as being indifferent or even positive about inflation.[111] Keynes had indeed expressed a preference for inflation over deflation, saying that if one has to choose between the two evils it is "better to disappoint the rentier" than to inflict pain on working-class families. However, Keynes was consistently adamant about the need to avoid inflation where possible.

In *The Economic Consequences of the Peace*, Keynes had written:

> Lenin is said to have declared that the best way to destroy the Capitalist System was to debauch the currency. By a continuing process of inflation, governments can confiscate, secretly and unobserved, an important part of the wealth of their citizens. There is no subtler, no surer means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose.

Keynes remained convinced of the dangers of inflation to the end of his life;[34] during World War II he argued strongly for policies that would minimise post-war inflation.

Personal life


Painter Duncan Grant with Keynes.

Keynes's early romantic and sexual relationships were almost exclusively with men.[112] At Eton and at Cambridge, Keynes had been prolific in his homosexual activity; significant among these early partners were Dilly Knox and Daniel Macmillan.[13][113] Keynes was open about his homosexual affairs, and between 1901 to 1915, kept separate diaries in which he tabulated his many sexual encounters.[114] Keynes's relationship and later close friendship with Macmillan was to be fortuitous; through Dan, Macmillan & Co first published his *Economic Consequences of the Peace*.[115] Attitudes in the Bloomsbury Group, in which Keynes was avidly involved, were relaxed about homosexuality. Keynes, together with writer Lytton Strachey, had reshaped the Victorian attitudes of the influential Cambridge Apostles; "since [their] time, homosexual relations among the members were for a time common", wrote Bertrand Russell.[116] One of Keynes's greatest loves was the artist Duncan Grant, whom he met in 1908. Like Grant, Keynes was also involved with Lytton Strachey,[112] though they were for the most part love rivals, and not lovers. Keynes had won the affections of Arthur Hobhouse,[117] as well as Grant, both times falling out with a jealous Strachey for it.[118] Strachey had previously found himself put off by Keynes, not least because of his manner of "treat[ing] his love affairs statistically".[119]

Ray Costelloe (who would later marry Oliver Strachey) was an early heterosexual interest of Keynes.[120] Of this infatuation, Keynes had written "I seem to have fallen in love with Ray a little bit, but as she isn't male I haven't [been] able to think of any suitable steps to take."[121]

Marriage

In 1921, Keynes fell "very much in love" with Lydia Lopokova, a well-known Russian ballerina, and one of the stars of Sergei Diaghilev's *Ballets Russes*. For the first years of the courtship, Keynes maintained an affair with a younger man, Sebastian Sprott, in tandem with Lopokova, but eventually chose Lopokova exclusively, on marrying her.[122][123] They married in 1925.[95][112] The union was happy, with biographer Peter Clarke writing that the marriage gave Keynes "a new focus, a new emotional stability and a sheer delight of which he never wearied".[124][125] Lydia became pregnant in 1927 but miscarried.[125] Among Keynes's Bloomsbury friends, Lopokova was, at least initially, subjected to criticism for her manners, mode of conversation and supposedly humble social origins – the latter of the ostensible causes being particularly noted in the letters of Vanessa and Clive Bell, and Virginia Woolf.[126][127] In her novel *Mrs Dalloway* (1925), Woolf bases the character of Rezia Warren Smith on Lopokova.[128] E. M. Forster would later write in contrition: "How we all used to underestimate her".[126]

Support for the arts

46 Gordon Square in London, where Keynes lived from 1916 to 1946.

nice place

Keynes was interested in literature in general and drama in particular and supported the Cambridge Arts Theatre financially, which allowed the institution, at least for a while, to become a major British stage outside of London.[95]

Keynes's personal interest in classical opera and dance led him to support the Royal Opera House at Covent Garden and the Ballet Company at Sadler's Wells. During the War as a member of CEMA (Council for the Encouragement of Music and the Arts) Keynes helped secure government funds to maintain both companies while their venues were shut. Following the War Keynes was instrumental in establishing the Arts Council of Great Britain and was the founding Chairman in 1946. Unsurprisingly from the start the two organisations that received the largest grant from the new body were the Royal Opera House and Sadler's Wells.

Like several other notable British authors of his time, Keynes was a member of the Bloomsbury Group. Virginia Woolf's biographer tells an anecdote on how Virginia Woolf, Keynes and T. S. Eliot would discuss religion at a dinner party, in the context of their struggle against Victorian era morality.[129] Keynes had attended church up to his teens,[130] but by university he had become agnostic, which he remained until his death.[131]

Investments

Keynes was ultimately a successful investor, building up a private fortune. His assets were nearly wiped out following the Stock Market Crash of 1929, which he failed to foresee, but he soon recouped. At Keynes's death, in 1946, his worth stood just short of £500,000 – equivalent to about £11 million ($16.5 million) in 2009. The sum had been amassed despite lavish support for various causes and his personal ethic which made him reluctant to sell on a falling market when if too many did it could deepen a slump.[132]

Keynes built up a substantial collection of fine art, including works, not all of them minor, by Paul Cézanne, Edgar Degas, Amedeo Modigliani, Georges Braque, Pablo Picasso, and Georges Seurat (some of which can now be seen at the Fitzwilliam Museum).[95] He enjoyed collecting books: for example, he collected and protected many of Isaac Newton's papers. It is in part on the basis of these papers that Keynes wrote of Newton as "the last of the magicians."[133]

Political causes

Keynes was a lifelong member of the Liberal party, which until the 1920s had been one of the two main political parties in the United Kingdom, and as late as 1916 had often been the dominant power in government. Keynes had helped campaign for the Liberals at elections from as early as 1906, yet he always refused to run for office himself, despite being asked to do so on three separate occasions in 1920. From 1926 when Lloyd George became leader of the Liberals, Keynes took a major role in defining the party's economics policy, but by then the Liberals had been displaced into third party status by the Labour party.[11]

In 1939 Keynes had the option to enter Parliament as an independent MP with the University of Cambridge seat. A by-election for the seat was to be held due to the illness of an elderly Tory, and the master of Magdalene College had obtained agreement that none of the major parties would field a candidate if Keynes chose to stand. Keynes declined the invitation as he felt he would wield greater influence on events if he remained a free agent.[125]

Keynes was a proponent of eugenics. He served as Director of the British Eugenics Society from 1937 to 1944. As late as 1946, shortly before his death, Keynes declared eugenics to be "the most important, significant and, I would add, genuine branch of sociology which exists."[134]

Keynes once remarked that "the youth had no religion save Communism and this was worse than nothing."[129] Marxism "was founded upon nothing better than a misunderstanding of Ricardo", and, given time, he, Keynes, "would deal thoroughly with the Marxists" and other economists to solve the economic problems their theories "threaten[ed] to cause".[129]

In 1931 Keynes went on to write the following on Marxism:[135]

> How can I accept the Communist doctrine, which sets up as its bible, above and beyond criticism, an obsolete textbook which I know not only to be scientifically erroneous but without interest or application to the modern world? How can I adopt a creed which, preferring the mud to the fish, exalts the boorish proletariat above the bourgeoisie and the intelligentsia, who with all their faults, are the quality of life and surely carry the seeds of all human achievement? Even if we need a religion, how can we find it in the turbid rubbish of the red bookshop? It is hard for an educated, decent, intelligent son of Western Europe to find his ideals here, unless he has first suffered some strange and horrid process of conversion which has changed all his values.

Death

Throughout his life Keynes worked energetically for the benefit both of the public and his friends – even when his health was poor he laboured to sort out the finances of his old college,[136] and at Bretton Woods, he worked to institute an international monetary system that would be beneficial for the world economy. Keynes suffered a series of heart attacks, which ultimately proved fatal, beginning during negotiations for an Anglo-American loan in Savannah, Georgia, where he was trying to secure favourable terms for the United Kingdom from the United States, a process he described as "absolute hell."[26][137] A few weeks after returning from the United States, Keynes died of a heart attack at Tilton, his farmhouse home near Firle, East Sussex, England, on 21 April 1946 at the age of 62.[11][138] Both of Keynes's parents outlived him: father John Neville Keynes (1852–1949) by three years, and mother Florence Ada Keynes (1861–1958) by 12 years. Keynes's brother Sir Geoffrey Keynes (1887–1982) was a distinguished surgeon, scholar and bibliophile. His nephews include Richard Keynes (1919–2010) a physiologist; and Quentin Keynes (1921–2003), an adventurer and bibliophile. His widow, Lydia Lopokova, lived on until 1981.

Publications

- 1913 *Indian Currency and Finance*
- 1914 *Ludwig von Mises's Theorie des Geldes* (EJ)
- 1915 *The Economics of War in Germany* (EJ)
- 1919 *The Economic Consequences of the Peace*
- 1921 *A Treatise on Probability*
- 1922 *The Inflation of Currency as a Method of Taxation* (MGCRE)
- 1922 *Revision of the Treaty*
- 1923 *A Tract on Monetary Reform*
- 1925 *Am I a Liberal?* (N&A)
- 1926 *The End of Laissez-Faire*
- 1926 *Laissez-Faire and Communism*
- 1930 *A Treatise on Money*
- 1930 *Economic Possibilities for our Grandchildren*
- 1931 *The End of the Gold Standard* (Sunday Express)
- 1931 *Essays in Persuasion*
- 1933 *An Open Letter to President Roosevelt* (New York Times)
- 1936 *The General Theory of Employment, Interest and Money*
- 1940 *How to Pay for the War: A radical plan for the Chancellor of the Exchequer*

See also

- Animal spirits (Keynes)
- Embedded liberalism
- Global financial system
- Post-war consensus
- Stockholm school (economics)

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Say's law

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Say's law, or the **law of market**, is an economic principle of classical economics named after the French businessman and economist Jean-Baptiste Say (1767–1832), who stated that "products are paid for with products"[1] and "a glut can take place only when there are ~~too many means of production~~ applied to one kind of product and not enough to another".[1]:178–9 In Say's view, a rational businessman will never hoard money; he will promptly spend any money he gets "for the value of money is also perishable."[1]:138–9

but that is not why

interest

Say's law was generally accepted throughout the 19th century, though modified to incorporate the idea of a "boom and bust" cycle, which was viewed as natural and inevitable. During the worldwide Great Depression, in the first half of the 20th century, a school of economics called Keynesian economics arose, disputing Say's conclusions. The debate between classical economics and Keynesian economics continues today.[2]

Say was not the discoverer of "Say's law", but the name appears to have stuck to the popularizer of this economic theory, which was in circulation at the dawn of the Industrial Revolution.[3]

Contents

Formulations

Say's formulation

In Say's language, "products are paid for with products" (1803: p. 153) or "a glut can take place only when there are too many means ~~of production applied~~ to one kind of product and not enough to another" (1803: p. 178-9). Explaining his point at length, he wrote that:

> It is worthwhile to remark that a product is no sooner created than it, from that instant, affords a

> market for other products to the full extent of its own value. When the producer has put the finishing hand to his product, he is most anxious to sell it immediately, lest its value should diminish in his hands. Nor is he less anxious to dispose of the money he may get for it; for the value of money is also perishable. But the only way of getting rid of money is in the purchase of some product or other. Thus the mere circumstance of creation of one product immediately opens a vent for other products. *(J. B. Say, 1803: pp.138–9)*[4]

So immediate market for products

He also wrote, that it is not the abundance of money but the abundance of other products in general that facilitates sales:

> Money performs but a momentary function in this double exchange; and when the transaction is finally closed, it will always be found, that one kind of commodity has been exchanged for another.[5]

Restatements

The Scottish economist James Mill restates Say's law in 1808, writing that "production of commodities creates, and is the one and universal cause which creates a market for the commodities produced."[6]

Say himself never used many of the later short definitions of Say's law and thus Say's law actually developed due to the work of many of his contemporaries and those who came after him. The work of James Mill, David Ricardo, John Stuart Mill, and others evolved Say's law into what is sometimes called "law of markets" which was the framework of macroeconomics from the mid-19th century until the 1930s.

Consequences

A number of laissez-faire consequences are drawn from interpretations of Say's law.

However, Say himself advocated public works to remedy unemployment, and criticized Ricardo for neglecting the possibility of hoarding if there was a lack of investment opportunities.[7]

Recession and unemployment

Say argued against claims that businesses suffer because people do not have enough money. Say argued that the power to purchase can only be increased by more production.

James Mill used Say's law against those who sought to give the economy a boost via unproductive consumption. In his view, consumption destroys wealth, in contrast to production which is the source of economic growth. The demand for a product determines the price of the product.

According to Keynes (see more below), if Say's law is correct, widespread involuntary unemployment (caused by inadequate demand) cannot occur. Classical economists in the context of Say's law explain unemployment as arising from insufficient demand for specialized labour. That is, supply of viable labour had exceeded demand in some segments of the economy.

Continuous cycle – then what did keynes say breaks it?

When more goods are produced by firms than demanded in certain sectors, the suppliers in those sectors lose revenue as result. This loss of revenue which would in turn been used to purchase other goods from other firms, lowers demand for the products of firms in other sectors, causing a overall general reduction in output, and thus lowering the demand for labour. This results in what contemporary macroeconomics call "structural unemployment", the presumed mismatch between overall demand for labour in jobs offered, and the individual job skills and location of labour. This differs from Keynesian "cyclical unemployment" that is presumed to arise because of inadequate aggregate demand. wait I don't see the contrast...

Such economic losses and unemployment were seen by some economists as an intrinsic property of the capitalistic system. Division of labor leads to a situation where one always has to anticipate what others will be willing to buy, and this will lead to miscalculations. However this theory alone does not explain the existence of cyclical phenomena in the economy because these miscalculations would happen with constant frequency, and to such a large scale that thousands of businesses in multiple sectors would simultaneously miscalculate (as during an economic bubble). ✓diff people w/ diff trades

Economists of the Austrian School, notably Ludwig von Mises, have linked these fluctuations in business cycles to the creation of central banking and its monopolized control of fiat money and prime interest rates. In their view, credit expansion, with central banking / Federal Reserves altering interest rates beyond what the free market would normally bear leads the market into malinvestment. This malinvestment creates the boom and bust bubble cycle, particularly in long-term sectors of the economy, such as in the recent United States housing bubble which has been linked to the Federal Reserve money/credit expansion of the 2001–2004 period (which itself was an emergency response intended to add liquidity into the market after the dot-com bubble collapsed).[8][9] According to laissez-faire economists such as Friedrich von Hayek, massive waves of unemployment, as in economic recessions and depressions, can be traced back to state intervention in the market, which effectively blocks the natural balance in means of production achieved through Say's law.

Assumptions and critiques

over simplification

Say's law did not posit that (as per the Keynesian formulation of Say's law) "supply creates its own demand". Neither was it based on the idea that all that is saved will be exchanged. Rather, Say sought to refute the idea that production and employment were limited by low consumption.

Thus Say's law, in its original concept, was not intrinsically linked nor logically reliant on the neutrality of money (as has been alleged by those who wish to disagree with the law[citation needed]) because the key proposition of the Law is that no matter how much people save, production is still a possibility as it is the prerequisite for the attainment of any additional goods of consumption. Say's law states that in a market economy, goods and services are produced for exchange with other goods and services – 'employment multipliers' – therefore arise from production and not exchange alone-and in the process a sufficient level of real income is created to purchase the economy's entire output due to the truism that the means of consumption are limited *ex vi termini* by the level of production. That is to say, (with regard exchange of produce within a division of labour) the total supply of goods and services in a market economy will equal the total demand derived from consumption during any given time period – in modern terms, "general gluts cannot exist",[10] although there may be local imbalances, with gluts in one market balanced by shortages in others.

Nevertheless, for some neoclassical economists, Say's law implies that economy is always at its full-employment level. This is not necessarily what was proposed by Say.

In the Keynesian interpretation,[citation needed] the assumptions of Say's law are:

- A barter model of money – "products are paid for with products;"
- Flexible prices – all prices can rapidly adjust upwards or downwards;
- No government intervention.

Under these assumptions, Say's law implies that there cannot be a general glut, so that a persistent state in which demand is generally less than productive capacity and high unemployment results, cannot exist. Keynesians therefore argued that the Great Depression demonstrated that Say's law is incorrect. Keynes, in his *General Theory*, argued that a country could go into a recession because of "lack of aggregate demand". [citation needed] Which is what? People save $ instead, ↓ consumption

Since there have been a great many persisting economic crises historically, one may either reject one or more of the assumptions of Say's law, its reasoning, or its conclusions. Taking the assumptions in turn:

- Circuitists and some post-Keynesians dispute the barter model of money, arguing that money is fundamentally different from commodities, and that credit bubbles can and do cause depressions. Notably, debt owed does not change because the economy has changed. ⟸ ahh nominal vs real
- Keynes argued that prices are not flexible – for example, workers may not take pay cuts if the result is starvation.[citation needed] in terms of how wages + debt denominated
- Laissez faire economists argue that government intervention is the cause of economic crises, and that left to its devices, the market will adjust efficiently.

Turning to the implication that dislocations cannot cause persistent unemployment, some theories of economic cycles accept Say's law, and seek to explain high unemployment in other ways, considering depressed demand for labor as a form of local dislocation. For example, Real Business Cycle Theory advocates[citation needed] argue that real shocks cause recessions, and that the market responds efficiently to these real economic shocks.

ie but higher / more steady std of living

Care for all or care from some?

Role of money

It is not easy to say what exactly Say's law says about the role of money apart from the claim that recession is not caused by lack of money. The phrase "products are paid for with products" is taken to mean that Say has a barter model of money; contrast with Circuitist and Post-Keynesian monetary theory.

One can read Say as stating simply that money is completely neutral, although Say did not state that explicitly, in fact did not concern himself with this subject. The central notion that Say had concerning money is this: if one has money, it is *irrational* to hoard it.[citation needed]

The assumption that hoarding is irrational was attacked by underconsumptionist economists, such as John M. Robertson, in his 1892 *The Fallacy of Saving*,[11][12] where he called Say's law:

> ...a tenacious fallacy, consequent on the inveterate evasion of the plain fact that men want for their goods, not merely some other goods to consume, but further, some credit or abstract claim to future wealth, goods, or services. This all want as a surplus or bonus, and this surplus cannot be represented for all in present goods.
>
> —John M. Robertson, *The Fallacy of Saving,* p. 98

Here Robertson identifies his critique as based on Say's theory of money – that people wish to accumulate a "claim to future wealth," not simply present goods, and thus hoarding of wealth may be rational.

To Say, as with other classical economists, it is quite possible for there to be a glut (excess supply, market surplus) for one product, and it co-exists with a shortage (excess demand) for others. But there is no "general glut" in Say's view, since the gluts and shortages cancel out for the economy as a whole. But what if the excess demand is for *money*, because people are hoarding it? This creates an excess supply for all products, a general glut. Say's answer is simple – there is no reason to engage in hoarding money. According to Say, the only reason to have money is to buy products. It would not be a mistake, in his view, to treat the economy *as if* it were a Barter economy. To quote Say:

> Nor is [an individual] less anxious to dispose of the money he may get ... But the only way of getting rid of money is in the purchase of some product or other.[*citation needed*]

An alternative modern view that gives an equivalent result is that all money that is held is done so in financial institutions (markets), so that any increase in the holding of money increases the supply of loanable funds. Then, with full adjustment of interest rates, the increased supply of loanable funds leads to an increase in borrowing and spending. So any negative effects on demand that results from the holding of money is canceled out and Say's law still applies.

In Keynesian terms, followers of Say's law would argue that on the aggregate level, there is only a transactions demand for money. That is, there is no precautionary, finance, or speculative demand for money. Money is held for spending and increases in money supplies lead to increased spending.

Some classical economists did see that loss of confidence in business or collapse of credit will increase the demand for money which would cut down the demand for goods. This view was expressed both by Robert Torrens[*citation needed*] and John Stuart Mill.[*citation needed*] This would lead demand and supply to move out of phase and lead to an economic downturn in the same way as miscalculation in productions, as described by William H. Beveridge in 1909. However, in classical economics, there was no reason for such a collapse to persist. Persistent depressions, such as that of the 1930s, are impossible in a free market according to *laissez-faire* principles. The flexibility of markets under *laissez faire* allow prices, wages, and interest rates to adjust to abolish all excess supplies and demands; however, since all economies are a mixture of regulation and free market elements, laissez-faire principles (which require a free market environment) would not be able to adjust effectively to excess supply and demand.

Say's law as a theoretical point of departure

The whole of Neoclassical equilibrium analysis implies that Say's law in the first place functioned to bring a market into this state – Say's law is the mechanism through which markets equilibrate uniquely. Equilibrium analysis and its derivatives of optimization and efficiency in exchange live or die with Say's law. This is one of the major points, if not *the* major point, of contention at perhaps the most fundamental level between the Neoclassical tradition, Keynes, and Marxians. Ultimately, from Say's law they deduced their vastly different conclusions as to the functioning of capitalist production.

The former, not to be confused with 'New Keynesian and the many offsprings and various syntheses of 'The General Theory', take the fact that a commodity-commodity economy is substantially altered in content once it becomes a commodity-money-commodity economy, or once money becomes not only a facilitator of exchange as is its only function in marginalist theory but a store of value and means of payment as well. What this means is simply that money can be (and must be) hoarded: it may not reenter the circulatory process for some time and thus a general glut is not only possible but, to the extent that money is not rapidly turned over, highly probable.

A response to this in defense of Say's law (echoing the debates between Ricardo and Malthus in which the former denied the possibility of a general glut on its grounds) is that consumption abstained from through the hoarding function is simply transferred to a different consumer – overwhelmingly to factor (investment) markets which, through financial institutions, function through the rate of interest.

Keynes' innovation in this regard was twofold:

First, he was to turn the mechanism which regulates savings and investment, the rate of interest, into a shell of its former self (relegating it to the *price of money*) by showing that supply and investment were not independent of one another and thus could not be related uniquely in terms of the balancing of dis-utility and utility.

Second, after Say's law was dealt with and shown to be theoretically inconsistent there was a gap to be filled – if Say's law was the logic by which we thought financial markets came to a unique position in the long run, and if Say's law were to be discarded, what were the 'rules of the game' of the financial markets; how did they function and how did they remain stable?

To this he responded with his famous notion of 'Animal Spirits' – that they were ruled by speculative behavior influenced not only by one's own personal equation but by his or her perceptions of the speculative behavior of others; in turn others behavior was motivated by their perceptions of others behavior, et al. Financial markets without Say's law keeping them in balance were thus inherently unstable, and through this identification Keynes deduced the consequences to the macro-economy of long run equilibrium being attained not at only one unique position which represented a 'Pareto Optima' (a special case), but through a possible range of many equilibria that could far under employ human and natural resources (the general case).

For the Marxian critique, which is more fundamental, one must start at Marx's distinction from the outset of use value and exchange value, use value being the use somebody has for an object, and exchange value being what an item is traded for on a market. In Marx's theory, there is a gap between the creation of surplus value in production, and the realisation of that surplus value via a sale. To realise a sale, an object must have a use-value for someone, in order so that they purchase the commodity, and complete the cycle of M-C-M'. Capitalism, which is purely interested in value (money as wealth), must create use value. The capitalist has no control over whether or not the value contained in their product is realised through the mechanism of the market. This gap in between production and realisation creates the possibility for capitalist crisis. As the realisation of capital is only possible through a market, Marx criticised other economists, such as David Ricardo, who argued that capital is realised via production. Thus, on Marx's theory, there can be *general* overproductive crises within capitalism.[13]

Once these concepts and their implications are understood it will become obvious why Say's law does not hold in the Marxian framework. Not only that, but the theoretical core of the Marxian framework's contrast with the Neoclassical and Austrian traditions will be clearly visible.

Conceptually, the distinction between Keynes and Marx is that for Keynes the theory is but a special case to his general theory, whereas for Marx it never existed at all.

Modern interpretations

A modern way of expressing Say's law is that there can never be a general glut. Instead of there being an excess supply (glut or surplus) of goods in general, there may be an excess supply of one or more goods but only when balanced by an excess demand (shortage) of yet other goods. Thus, there may be a glut of labor ("cyclical" unemployment), but that is balanced by an excess demand for produced goods. Modern advocates of Say's law see market forces as working quickly – via price adjustment – to abolish both gluts and shortages. The exception would be the case where the government or other non-market forces prevent price changes.

According to Keynes, the implication of Say's "law" is that a free-market economy is always at what the Keynesian economists call full employment; see also Walras' law. Thus, Say's law is part of the general world-view of laissez-faire economics, i.e., that free markets can solve the economy's problems automatically. (Here the problems are recessions, stagnation, depression, and involuntary unemployment.)

Some proponents of Say's law argue that such intervention is always counterproductive. Consider Keynesian-type policies aimed at stimulating the economy. Increased government purchases of goods (or lowered taxes) merely "crowds out" the private sector's production and purchase of goods. Contradicting this view, Arthur Cecil Pigou – a self-proclaimed follower of Say's law – wrote a letter in 1932 signed by five other economists (among them Keynes) calling for more public spending to alleviate high levels of unemployment.

Keynes vs. Say

For more details on this topic, see Supply creates its own demand.

Keynes summarized Say's law as "supply creates its own demand", which is to say, the assumption "that the whole of the costs of production must necessarily be spent in the aggregate, directly or indirectly, on purchasing the product" (from Chapter Two of his *General Theory*).

Keynesian economists stress the role of money in negating Say's law: Money that is hoarded (held as cash or analogous financial instruments) is not spent on products. To increase monetary holdings, someone may sell products or labor without immediately spending the proceeds. This can be a general phenomenon: From time to time, in response to changing economic circumstances, households and businesses in aggregate seek to increase net savings and thus decrease net debt. To increase net savings requires earning more than is spent, contrary to Say's Law, which postulates that supply (sales earning income) equals demand (purchases requiring spending). Keynesian economists argue that the failure of Say's Law, through increased demand for monetary holdings, can result in a general glut due to falling demand for goods and services.

ie Savings

This provides an explanation for recessionary spirals and economic depressions. Without sufficient demand for the products of labor, the availability of jobs will be low; without enough jobs, working people will receive inadequate income, implying insufficient demand for products. Thus, an aggregate demand failure involves a vicious circle: if one supplies more of his labor-time (in order to buy more goods), he may be frustrated because no-one is hiring – because there is no increase in the demand for their products until *after* he gets a job and earns an income. (Of course, most get paid after working, which occurs after some of the product is sold.) Note also that unlike the Say's law story above, there are interactions between different markets (and their gluts and shortages) that go beyond the simple price mechanism, to limit the quantity of jobs supplied and the quantity of products demanded.

Some classical economists suggested that hoarding (increases in money-equivalent holdings) would always be balanced by dishoarding. This requires equality of saving (abstention from purchase of goods) and investment (the purchase of capital goods). However, Keynes and others argued that hoarding decisions are made by different people and for different reasons than decisions to dishoard, so that hoarding and dishoarding are unlikely to be equal at all times, as indeed they are not. Decreasing demand (consumption) does not necessarily stimulate capital spending (investment).

Some have argued that financial markets and especially interest rates could adjust to keep hoarding and dishoarding equal, so that Say's law could be maintained, or that prices could simply fall, to prevent a decrease in production. (See the discussion of "excess saving" under "Keynesian economics".) But Keynes argued that in order to play this role, interest rates would have to fall rapidly and that there were limits on how quickly and how low they could fall (as in the liquidity trap, where interest rates approach zero and cannot fall further). To Keynes, in the short run, interest rates were determined more by the supply and demand for money than by saving and investment. Before interest rates could adjust sufficiently, excessive hoarding would cause the vicious circle of falling aggregate production (recession). The recession itself would lower incomes so that hoarding (and saving) and dishoarding (and real investment) could attain balance below full employment.

Worse, a recession would hurt private real investment – by hurting profitability and business confidence – in what is called the accelerator effect. This means that the balance between hoarding and dishoarding would be pushed even further below the full employment level of production.

expectations

Keynesians[citation needed] argue that this kind of vicious circle can be broken by stimulating the aggregate demand for products using various macroeconomic policies mentioned in the introduction above, making Say's law true in practice when it is false in theory[2] (http://delong.typepad.com/sdj/economic_history/page/4/) . Increases in the demand for products leads to increased supply (production) and an increased availability of jobs, and thus further increases in demand and in production. This cumulative causation is called the multiplier process.

See also

- Fiscal policy
- List of eponymous laws
- Parable of the broken window
- Treasury view, a related critical view of fiscal policy
- Walras' law

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Notes

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Keynesian economics

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Keynesian economics (/ˈkeɪnziən/ *KAYN-zee-ən*; also called **Keynesianism** and **Keynesian theory**) are the group of macroeconomic schools of thought based on the ideas of 20th-century economist John Maynard Keynes. Keynesian economists believe that in the short run, productive activity is influenced by aggregate demand (total spending in the economy) and that aggregate demand does not necessarily equal aggregate supply (the total productive capacity of the economy). Instead it is influenced by a host of factors and sometimes behaves erratically, affecting production, employment and inflation.[1]

Advocates of Keynesian economics argue that private sector decisions sometimes lead to inefficient macroeconomic outcomes which require active policy responses by the public sector, particularly monetary policy actions by the central bank and fiscal policy actions by the government to stabilize output over the business cycle.[2] The theories forming the basis of Keynesian economics were first presented by Keynes in his book, *The General Theory of Employment, Interest and Money,* published in 1936. The interpretations of Keynes are contentious and several schools of thought claim his legacy.

Keynesian economics advocates a mixed economy – predominantly private sector, but with a role of for government intervention during recessions – and in the USA served as the standard economic model during the later part of the Great Depression, World War II, and the post-war economic expansion (1945–1973), though it lost some influence following the tax surcharge in 1968 and the stagflation of the 1970s.[3] The advent of the global financial crisis in 2008 has caused a resurgence in Keynesian thought.[4]

Contents

Theory

Prior to the publication of Keynes' General Theory, mainstream economic thought was that the economy existed in a state of general equilibrium, meaning that the economy naturally consumes whatever it produces because the needs of consumers are always greater than the capacity of the economy to satisfy those needs. This perception is reflected in Say's Law[5] and in the writing of David Ricardo,[6] which is that individuals produce so that they can either consume what they have manufactured or sell their output so that they can buy someone else's output. This perception rests upon the assumption that if a surplus of goods or services exists, they would naturally fall in price to the point where they would be consumed.

Keynes' theory was significant because it overturned the mainstream thought of the time and brought about a greater awareness that problems such as unemployment are not a product of laziness, but the result of a structural inadequacy in the economic system. He argued that because there was no guarantee that the goods that individuals produce would be met with demand, unemployment was a natural consequence. He saw the economy as unable to maintain itself in equilibrium and believed that it was necessary for the government to step in and put under-utilised savings to work through government spending. Thus, according to Keynesian theory, some individually-rational microeconomic-level actions such as not investing savings in the goods and services produced by the economy, if taken collectively by a large proportion of individuals and firms, can lead to outcomes, wherein the economy operates below its potential output and growth rate.

Prior to Keynes, a situation in which aggregate demand for goods and services did not meet supply was referred to by classical economists as a *general glut*, although there was disagreement among them as to whether a general glut was possible. Keynes argued that when a glut occurred, it was the over-reaction of producers and the laying off of workers that led to a fall in demand and perpetuating the problem. Keynesians therefore advocate an active stabilization policy to reduce the amplitude of the business cycle, which they rank among the most serious of economic problems. According to the theory, government spending can be used to increase aggregate demand, thus increasing economic activity, reducing unemployment and deflation.

Keynes argued that the solution to the Great Depression was to stimulate the economy ("inducement to invest") through some combination of two approaches:

1. A reduction in interest rates (monetary policy), and
2. Government investment in infrastructure (fiscal policy).

By reducing the interest rate at which the central bank lends money to commercial banks, the government sends a signal to commercial banks that they should do the same for their customers. In reality, government loans to commercial banks make up a tiny proportion of the overall funding of commercial banks, and as a consequence, it can be ineffective at times when the degree of economic contraction is significant.

but signal

Investment by government in infrastructure injects income into the economy by creating business opportunity, employment and demand and reversing the effects of the aforementioned imbalance.[7] Governments source the funding for this expenditure by borrowing funds from the economy through the issue of government bonds, and because government spending exceeds the amount of tax income that the government receives, this creates a fiscal deficit.

A central conclusion of Keynesian economics is that, in some situations, no strong automatic mechanism moves output and employment towards full employment levels. This conclusion conflicts with economic approaches that assume a strong general tendency towards equilibrium. In the 'neoclassical synthesis', which combines Keynesian macro concepts with a micro foundation, the conditions of general equilibrium allow for price adjustment to eventually achieve this goal. More broadly, Keynes saw his theory as a *general* theory, in which utilization of resources could be high or low, whereas previous economics focused on the *particular* case of full utilization.

The new classical macroeconomics movement, which began in the late 1960s and early 1970s, criticized Keynesian theories, while New Keynesian economics has sought to base Keynes's ideas on more rigorous theoretical foundations.

Some interpretations of Keynes have emphasized his stress on the international coordination of Keynesian policies, the need for international economic institutions, and the ways in which economic forces could lead to war or could promote peace.[8]

Concepts

Wages and spending

During the Great Depression, the classical theory defined economic collapse as simply a lost incentive to produce, and the mass unemployment as a result of high and rigid real wages.[*citation needed*]

To Keynes, the determination of wages is more complicated. First, he argued that it is not *real* but *nominal* wages that are set in negotiations between employers and workers, as opposed to a barter relationship. Second, nominal wage cuts would be difficult to put into effect because of laws and wage contracts. Even classical economists admitted that these exist; unlike Keynes, they advocated abolishing minimum wages, unions, and long-term contracts, increasing labour-market flexibility. However, to Keynes, people will resist nominal wage reductions, even without unions, until they see other wages falling and a general fall of prices.

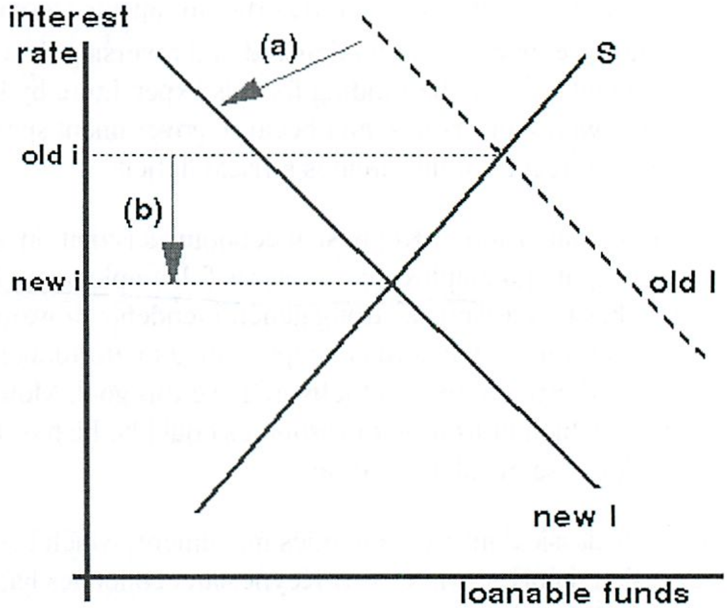
Keynes rejected the idea that cutting wages would cure recessions. He examined the explanations for this idea and found them all faulty. He also considered the most likely consequences of cutting wages in recessions, under various different circumstances. He concluded that such wage cutting would be more likely to make recessions worse rather than better.[9]

read

Further, if wages and prices were falling, people would start to expect them to fall. This could make the economy spiral downward as those who had money would simply wait as falling prices made it more valuable—rather than spending. As Irving Fisher argued in 1933, in his *Debt-Deflation Theory of Great Depressions*, deflation (falling prices) can make a depression deeper as falling prices and wages made pre-existing nominal debts more valuable in real terms.

Exactly

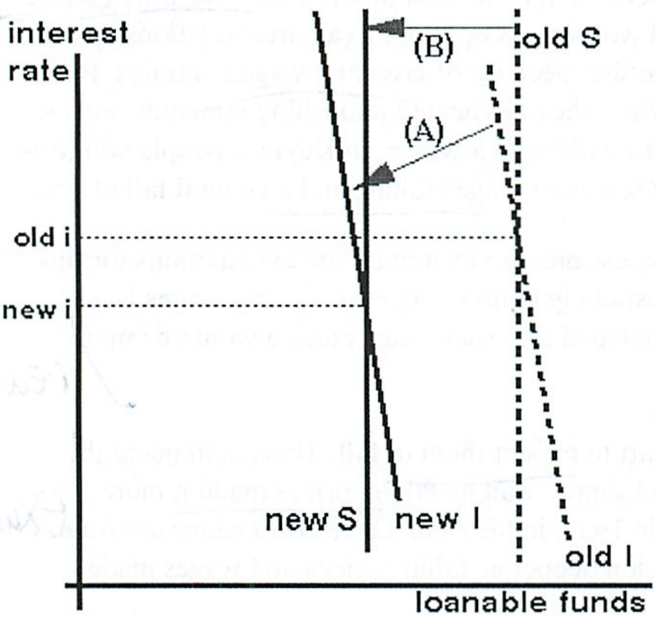
Excessive saving



To Keynes, excessive saving, i.e. saving beyond planned investment, was a serious problem, encouraging recession or even depression. Excessive saving results if investment falls, perhaps due to falling consumer demand, over-investment in earlier years, or pessimistic business expectations, and if saving does not immediately fall in step, the economy would decline.

The classical economists argued that interest rates would fall due to the excess supply of "loanable funds". The first diagram, adapted from the only graph in *The General Theory*, shows this process. (For simplicity, other sources of the demand for or supply of funds are ignored here.) Assume that fixed investment in capital goods falls from "**old I**" to "**new I**" (step **a**). Second (step **b**), the resulting excess of saving causes interest-rate cuts, abolishing the excess supply: so again we have saving (**S**) equal to investment. The interest-rate (**i**) fall prevents that of production and employment.

Keynes had a complex argument against this *laissez-faire* response. The graph below summarizes his argument, assuming again that fixed investment falls (step **A**). *First*, saving does not fall much as interest rates fall, since the income and substitution effects of falling rates go in conflicting directions. *Second*, since planned fixed investment in plant and equipment is based mostly on long-term expectations of future profitability, that spending does not rise much as interest rates fall. So **S** and **I** are drawn as steep (inelastic) in the graph. Given the inelasticity of both demand and supply, a *large* interest-rate fall is needed to close the saving/investment gap. As drawn, this requires a *negative* interest rate at equilibrium (where the **new I** line would intersect the **old S** line). However, this negative interest rate is not necessary to Keynes's argument.



Third, Keynes argued that saving and investment are not the main determinants of interest rates, especially in the short run. Instead, the supply of and the demand for the stock of *money* determine interest rates in the short run. (This is not drawn in the graph.) Neither changes quickly in response to excessive saving to allow fast interest-rate adjustment.

Finally, Keynes suggested that, because of fear of capital losses on assets besides money, there may be a "liquidity trap" setting a floor under which interest rates cannot fall. While in this trap, interest rates are so low that any increase in money supply will cause bond-holders (fearing rises in interest rates and hence capital losses on their bonds) to sell their bonds to attain money (liquidity). In the diagram, the equilibrium suggested by the **new I** line and the **old S** line cannot be reached, so that excess saving persists. Some (such as Paul Krugman) see this latter kind of liquidity trap as prevailing in Japan in the 1990s. Most economists agree that nominal interest rates cannot fall below zero.

However, some economists (particularly those from the Chicago school) reject the existence of a liquidity trap.

Why/how?

Even if the liquidity trap does not exist, there is a *fourth* (perhaps most important) element to Keynes's critique. Saving involves not spending all of one's income. Thus, it means insufficient demand for business output, unless it is balanced by other sources of demand, such as fixed investment. Therefore, *excessive* saving corresponds to an unwanted accumulation of inventories, or what classical economists called a general glut.[10] This pile-up of unsold goods and materials encourages businesses to decrease both production and employment. This in turn lowers people's incomes—and saving, causing a leftward shift in the **S** line in the diagram (step **B**). For Keynes, the fall in income did most of the job by ending excessive saving and allowing the loanable funds market to attain equilibrium. Instead of interest-rate adjustment solving the problem, a recession does so. Thus in the diagram, the interest-rate change is small.

Whereas the classical economists assumed that the level of output and income was constant and given at any one time (except for short-lived deviations), Keynes saw this as the key variable that adjusted to equate saving and investment.

Finally, a recession undermines the business incentive to engage in fixed investment. With falling incomes and demand for products, the desired demand for factories and equipment (not to mention housing) will fall. This accelerator effect would shift the **I** line to the left again, a change not shown in the diagram above. This recreates the problem of excessive saving and encourages the recession to continue.

In sum, to Keynes there is interaction between excess supplies in different markets, as unemployment in labour markets encourages excessive saving—and *vice-versa*. Rather than prices adjusting to attain equilibrium, the main story is one of quantity adjustment allowing recessions and possible attainment of underemployment equilibrium.

Active fiscal policy

As noted, the classicals wanted to balance the government budget. To Keynes, this would exacerbate the underlying problem: following either the expansionary policy or the contractionary policy would *raise saving* (broadly defined) and thus lower the demand for both products and labour. For example, Keynesians would advise tax cuts instead.[11]

but opposite at good times

Keynes' ideas influenced Franklin D. Roosevelt's view that insufficient buying-power caused the Depression. During his presidency, Roosevelt adopted some aspects of Keynesian economics, especially after 1937, when, in the depths of the Depression, the United States suffered from recession yet again following fiscal contraction. But to many the true success of Keynesian policy can be seen at the onset of World War II, which provided a kick to the world economy, removed uncertainty, and forced the rebuilding of destroyed capital. Keynesian ideas became almost official in social-democratic Europe after the war and in the U.S. in the 1960s.

Keynes developed a theory which suggested that active government policy could be effective in managing the economy. Rather than seeing unbalanced government budgets as wrong, Keynes advocated what has been called countercyclical fiscal policies, that is, policies that acted against the tide of the business cycle: deficit spending when a nation's economy suffers from recession or when recovery is long-delayed and unemployment is persistently high—and the suppression of inflation in boom times by either increasing taxes or cutting back on government outlays. He argued that governments should solve problems in the short run

Economics 101

rather than waiting for market forces to do it in the long run, because, "in the long run, we are all dead."[12]

This contrasted with the classical and neoclassical economic analysis of fiscal policy. Fiscal stimulus (deficit spending) could actuate production. But, to these schools, there was no reason to believe that this stimulation would outrun the side-effects that "crowd out" private investment: first, it would increase the demand for labour and raise wages, hurting profitability; Second, a government deficit increases the stock of government bonds, reducing their market price and encouraging high interest rates, making it more expensive for business to finance fixed investment. Thus, efforts to stimulate the economy would be self-defeating. to what extent

but not if unemp

The Keynesian response is that such fiscal policy is appropriate only when unemployment is persistently high, above the non-accelerating inflation rate of unemployment (NAIRU). In that case, crowding out is minimal. Further, private investment can be "crowded in": Fiscal stimulus raises the market for business output, raising cash flow and profitability, spurring business optimism. To Keynes, this accelerator effect meant that government and business could be *complements* rather than substitutes in this situation. Second, as the stimulus occurs, gross domestic product rises, raising the amount of saving, helping to finance the increase in fixed investment. Finally, government outlays need not always be wasteful: government investment in public goods that will not be provided by profit-seekers will encourage the private sector's growth. That is, government spending on such things as basic research, public health, education, and infrastructure could help the long-term growth of potential output.

In Keynes's theory, there must be significant slack in the labour market before fiscal expansion is justified. Both conservative and some neoliberal economists question this assumption, unless labour unions or the government "meddle" in the free market, creating persistent supply-side or classical unemployment. Their solution is to increase labour-market flexibility, e.g., by cutting wages, busting unions, and deregulating business.

Contrary to some critical characterizations of it, Keynesianism does not consist solely of deficit spending. Keynesianism recommends counter-cyclical policies.[13] An example of a counter-cyclical policy is raising taxes to cool the economy and to prevent inflation when there is abundant demand-side growth, and engaging in deficit spending on labour-intensive infrastructure projects to stimulate employment and stabilize wages during economic downturns. Classical economics, on the other hand, argues that one should *cut* taxes when there are budget surpluses, and cut spending—or, less likely, increase taxes—during economic downturns. Keynesian economists believe that adding to profits and incomes during boom cycles through tax cuts, and removing income and profits from the economy through cuts in spending and/or increased taxes during downturns, tends to exacerbate the negative effects of the business cycle. This effect is especially pronounced when the government controls a large fraction of the economy, and is therefore one reason fiscal conservatives advocate a much smaller government.

"Multiplier effect" and interest rates

Main article: Spending multiplier

Two aspects of Keynes's model has implications for policy:

First, there is the "Keynesian multiplier", first developed by Richard F. Kahn in 1931. Exogenous increases in spending, such as an increase in government outlays, increases total spending by a multiple of that increase. A government could stimulate a great deal of new production with a modest outlay if:

1. The people who receive this money then spend most on consumption goods and save the rest.
2. This extra spending allows businesses to hire more people and pay them, which in turn allows a further increase in consumer spending.

This process continues. At each step, the increase in spending is smaller than in the previous step, so that the multiplier process tapers off and allows the attainment of an equilibrium. This story is modified and moderated if we move beyond a "closed economy" and bring in the role of taxation: The rise in imports and tax payments at each step reduces the amount of induced consumer spending and the size of the multiplier effect.

Second, Keynes re-analyzed the effect of the interest rate on investment. In the classical model, the supply of funds (saving) determines the amount of fixed business investment. That is, under the classical model, since all savings are placed in banks, and all business investors in need of borrowed funds go to banks, the amount of savings determines the amount that is available to invest. Under Keynes's model, the amount of investment is determined independently by long-term profit expectations and, to a lesser extent, the interest rate. The latter opens the possibility of regulating the economy through money supply changes, via monetary policy. Under conditions such as the Great Depression, Keynes argued that this approach would be relatively ineffective compared to fiscal policy. But, during more "normal" times, monetary expansion can stimulate the economy.[*citation needed*]

IS/LM model

The IS/LM model is nearly as influential as Keynes's original analysis in determining actual policy and economics education. It relates aggregate demand and employment to three exogenous quantities, i.e., the amount of money in circulation, the government budget, and the state of business expectations. This model was very popular with economists after World War II because it could be understood in terms of general equilibrium theory. This encouraged a much more static vision of macroeconomics than that described above.[*citation needed*]

Phillips curve

The second main part of a Keynesian policy-maker's theoretical apparatus was the Phillips curve. This curve, which was more of an empirical observation than a theory, indicated that increased employment, and decreased unemployment, implied increased inflation. Keynes had only predicted that falling unemployment would cause a higher price, not a higher inflation rate. Thus, the economist could use the IS-LM model to predict, for example, that an increase in the money supply would raise output and employment—and then use the Phillips curve to predict an increase in inflation.[*citation needed*]

History

Precursors

Keynes's work was part of a long-running debate within economics over the existence and nature of general gluts. While a number of the policies Keynes advocated (the notable one being government deficit spending at times of low private investment or consumption) and the theoretical ideas he proposed (effective demand, the multiplier, the paradox of thrift) were advanced by various authors in the 19th and early 20th centuries, Keynes's unique contribution was to provide a *general theory* of these, which proved acceptable to the political and economic establishments.

Schools

See also: Underconsumption, Birmingham School (economics), and Stockholm school (economics)

An intellectual precursor of Keynesian economics was underconsumption theory in classical economics, dating from such 19th-century economists as Thomas Malthus, the Birmingham School of Thomas Attwood,[14] and the American economists William Trufant Foster and Waddill Catchings, who were influential in the 1920s and 1930s. Underconsumptionists were, like Keynes after them, concerned with failure of aggregate demand to attain potential output, calling this "underconsumption" (focusing on the demand side), rather than "overproduction" (which would focus on the supply side), and advocating economic interventionism. Keynes specifically discussed underconsumption (which he wrote "under-consumption") in the *General Theory,* in Chapter 22, Section IV (http://www.marxists.org/reference/subject/economics/keynes/general-theory/ch22.htm#iv) and Chapter 23, Section VII (http://www.marxists.org/reference/subject/economics/keynes/general-theory/ch23.htm#vii) .

Numerous concepts were developed earlier and independently of Keynes by the Stockholm school during the 1930s; these accomplishments were described in a 1937 article, published in response to the 1936 *General Theory,* sharing the Swedish discoveries.[15]

Concepts

The multiplier dates to work in the 1890s by the Australian economist Alfred De Lissa, the Danish economist Julius Wulff, and the German American economist Nicholas Johannsen,[16] the latter being cited in a footnote of Keynes.[17] Nicholas Johannsen also proposed a theory of effective demand in the 1890s.

The paradox of thrift was stated in 1892 by John M. Robertson in his *The Fallacy of Savings,* in earlier forms by mercantilist economists since the 16th century, and similar sentiments date to antiquity.[18][19]

Today these ideas, regardless of provenance, are referred to in academia under the rubric of "Keynesian economics", due to Keynes's role in consolidating, elaborating, and popularizing them.

Keynes and the classics

Keynes sought to distinguish his theories from and oppose them to "classical economics," by which he meant the economic theories of David Ricardo and his followers, including John Stuart Mill, Alfred Marshall, Francis Ysidro Edgeworth, and Arthur Cecil Pigou. A central tenet of the classical view, known as Say's law, states that "supply creates its own demand." Say's Law can be interpreted in two ways. First, the claim that the total value of output is equal to the sum of income earned in production is a result of a national income accounting identity, and is therefore indisputable. A second and stronger claim, however, that the "*costs* of output are always covered in the aggregate by the sale-proceeds resulting from demand" depends on how consumption and saving are linked to production and investment. In particular, Keynes argued that the second, strong form of Say's Law only holds if increases in individual savings exactly match an increase in aggregate investment.[20]

Keynes sought to develop a theory that would explain determinants of saving, consumption, investment and production. In that theory, the interaction of aggregate demand and aggregate supply determines the level of output and employment in the economy.

Because of what he considered the failure of the "Classical Theory" in the 1930s, Keynes firmly objects to its main theory—adjustments in prices would automatically make demand tend to the full employment level.

Neo-classical theory supports that the two main costs that shift demand and supply are labour and money. Through the distribution of the monetary policy, demand and supply can be adjusted. If there were more labour than demand for it, wages would fall until hiring began again. If there were too much saving, and not enough consumption, then interest rates would fall until people either cut their savings rate or started borrowing.

Military Keynesianism

Main article: Military Keynesianism

is it military spending fixes?

Postwar Keynesianism

Main articles: Neo-Keynesian economics, New Keynesian economics, and Post-Keynesian economics

Keynes's ideas became widely accepted after WWII, and until the early 1970s, Keynesian economics provided the main inspiration for economic policy makers in Western industrialized countries.[3] Governments prepared high quality economic statistics on an ongoing basis and tried to base their policies on the Keynesian theory that had become the norm. In the early era of new liberalism and social democracy, most western capitalist countries enjoyed low, stable unemployment and modest inflation, an era called the Golden Age of Capitalism.

In terms of policy, the twin tools of post-war Keynesian economics were fiscal policy and monetary policy. While these are credited to Keynes, others, such as economic historian David Colander, argue that they are, rather, due to the interpretation of Keynes by Abba Lerner in his theory of Functional Finance, and should instead be called "Lernerian" rather than "Keynesian".[21]

Through the 1950s, moderate degrees of government demand leading industrial development, and use of fiscal and monetary counter-cyclical policies continued, and reached a peak in the "go go" 1960s, where it seemed to many Keynesians that prosperity was now permanent. In 1971, Republican US President Richard Nixon even proclaimed "we are all Keynesians now".[22] However, with the oil shock of 1973, and the economic problems of the 1970s, modern liberal economics began to fall out of favor. During this time, many economies experienced high and rising unemployment, coupled with high and rising inflation, contradicting the Phillips curve's prediction. This stagflation meant that the simultaneous application of expansionary (anti-recession) and contractionary (anti-inflation) policies appeared to be necessary. This dilemma led to the end of the Keynesian near-consensus of the 1960s, and the rise throughout the 1970s of ideas based upon more classical analysis, including monetarism, supply-side economics,[22] and new classical economics. At the same time, Keynesians began during the period to reorganize their thinking (some becoming associated with New Keynesian economics); one strategy, utilized also as a critique of the notably high unemployment and potentially disappointing GNP growth rates associated with the latter two theories by the mid-1980s, was to emphasize low unemployment and maximal economic growth at the cost of somewhat higher inflation (its consequences kept in check by indexing and other methods, and its overall rate kept lower and steadier by such potential policies as Martin Weitzman's share economy).[23]

Multiple schools of economic thought that trace their legacy to Keynes currently exist, the notable ones being Neo-Keynesian economics, New Keynesian economics, and Post-Keynesian economics. Keynes's biographer Robert Skidelsky writes that the post-Keynesian school has remained closest to the spirit of Keynes's work in following his monetary theory and rejecting the neutrality of money.[24][25]

In the postwar era, Keynesian analysis was combined with neoclassical economics to produce what is generally termed the "neoclassical synthesis", yielding Neo-Keynesian economics, which dominated mainstream macroeconomic thought. Though it was widely held that there was no strong automatic tendency to full employment, many believed that if government policy were used to ensure it, the economy would behave as neoclassical theory predicted. This post-war domination by Neo-Keynesian economics was broken during the stagflation of the 1970s. There was a lack of consensus among macroeconomists in the 1980s. However, the advent of New Keynesian economics in the 1990s, modified and provided microeconomic foundations for the neo-Keynesian theories. These modified models now dominate mainstream economics.

Post-Keynesian economists, on the other hand, reject the neoclassical synthesis and, in general, neoclassical economics applied to the macroeconomy. Post-Keynesian economics is a heterodox school that holds that both Neo-Keynesian economics and New Keynesian economics are incorrect, and a misinterpretation of Keynes's ideas. The Post-Keynesian school encompasses a variety of perspectives, but has been far less influential than the other more mainstream Keynesian schools.

Relationship to other schools of economics

The Keynesian schools of economics are situated alongside a number of other schools that have the same perspectives on what the economic issues are, but differ on what causes them and how to best resolve them:

Monetarism

Monetarists and Keynesians are in agreement over the fact that issues such as business cycles, unemployment, inflation need to be addressed, but have fundamentally different perspectives on the capacity of the economy to find its own equilibrium and as a consequence the degree of government intervention that is required to create equilibrium. Keynesians advocate that when the economy is experiencing a decline in confidence that governments should borrow under-employed savings from the economy and spend it on infrastructure, while monetarists argue that governments should balance their budgets and regulate the supply of money through interest rates.

Keynesian policies fell out of favour in the 1970's when it was realised that government spending was leading to inflation rather than create the economic stimulation that was required. Monetarism then became the dominant economic school and as a consequence, inflation rates fell across most developed countries and since the 1980's have remained significantly lower than they were in the 1970's. The Global Financial Crisis, however, has highlighted the need for Keynesian type government intervention through spending as governments found it impossible to stimulate economies through monetary policy alone.

Austrian economics

Austrian economists are more closely aligned with monetarists in that they favour diminished government intervention in the economy. They have a particular interests in the business cycle, arguing that economic booms are caused by excessive and unsustainable credit expansion to businesses and individual borrowers by the banks.[26] The excess supply of funds to capital tends to cause capital goods prices to rise and stimulates an unsustainable shift of investment from consumer goods to capital goods. The bidding up of house prices due to the abundance of credit prior to the Global Financial Crisis add credibility to the Austrian perspective, but does not form part of the mainstream thought.

Stockholm School

The Stockholm School rose to prominence at about the same time that Keynes published his General Theory and shared a common concern in business cycles and unemployment. The second generation of Swedish economists also advocated government intervention through spending during economic downturns[27] although opinions are divided over whether they conceived the essence of Keynes' theory before he did.[28]

Criticisms

Austrian School criticisms

Austrian economist Friedrich Hayek criticized Keynesian economic policies for what he called their fundamentally "collectivist" approach, arguing that such theories encourage centralized planning, which leads to malinvestment of capital, which is the cause of business cycles. Hayek also argued that Keynes's study of the aggregate relations in an economy is fallacious, as recessions are caused by micro-economic factors. Hayek claimed that what starts as temporary governmental fixes usually become permanent and expanding government programs, which stifle the private sector and civil society.[29]

Austrian economist Henry Hazlitt criticized, paragraph by paragraph, Keynes's *General Theory* in *The Failure of the New Economics*.[30]

New Classical Macroeconomics criticisms

See also: Lucas critique

Another influential school of thought was based on the Lucas critique of Keynesian economics. This called for greater consistency with microeconomic theory and rationality, and in particular emphasized the idea of rational expectations. Lucas and others argued that Keynesian economics required remarkably foolish and short-sighted behavior from people, which totally contradicted the economic understanding of their behavior at a micro level. New classical economics introduced a set of macroeconomic theories that were based on optimising microeconomic behavior. These models have been developed into the Real Business Cycle Theory, which argues that business cycle fluctuations can to a large extent be accounted for by real (in contrast to nominal) shocks.

Beginning in the late 1950s new classical macroeconomists began to disagree with the methodology employed by Keynes and his successors. Keynesians emphasized the dependence of consumption on disposable income and, also, of investment on current profits and current cash flow. In addition, Keynesians posited a Phillips curve that tied nominal wage inflation to unemployment rate. To support these theories, Keynesians typically traced the logical foundations of their model (using introspection) and supported their assumptions with statistical evidence.[31] New classical theorists demanded that macroeconomics be grounded on the same foundations as microeconomic theory, profit-maximizing firms and rational, utility-maximizing consumers.[31]

The result of this shift in methodology produced several important divergences from Keynesian Macroeconomics:[31]

1. Independence of Consumption and current Income (life-cycle permanent income hypothesis)
2. Irrelevance of Current Profits to Investment (Modigliani-Miller theorem)
3. Long run independence of inflation and unemployment (natural rate of unemployment)
4. The inability of monetary policy to stabilize output (rational expectations)
5. Irrelevance of Taxes and Budget Deficits to Consumption (Ricardian Equivalence)

See also

- 2008–2009 Keynesian resurgence
- Aggregate demand
- Functional finance
- Job guarantee

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John Maynard Keynes

The General Theory of Employment, Interest and Money

Read 10/28

Book I

Introduction

Chapter 1
The General Theory

I HAVE called this book the *General Theory of Employment, Interest and Money*, placing the emphasis on the prefix *general*. The object of such a title is to contrast the character of my arguments and conclusions with those of the *classical*[1] theory of the subject, upon which I was brought up and which dominates the economic thought, both practical and theoretical, of the governing and academic classes of this generation, as it has for a hundred years past. I shall argue that the postulates of the classical theory are applicable to a special case only and not to the general case, the situation which it assumes being a limiting point of the possible positions of equilibrium. Moreover, the characteristics of the special case assumed by the classical theory happen not to be those of the economic society which we actually live, with the result that its teaching is misleading and disastrous if we attempt to apply it to the facts of experience.

Author's Footnotes

1. "The classical economists" was a name invented by Marx to cover Ricardo and James Mill and their *predecessors,* that is to say for the founders of the theory which culminated in the Ricardian economics. I have become accustomed, perhaps perpetrating a solecism, to include in "the classical school" the *followers* of Ricardo, those, that is to say, who adopted and perfected the theory of the Ricardian economics, including (for example) J. S. Mill, Marshall, Edgeworth and Prof. Pigou. names silly

— like "Modern" Art

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John Maynard Keynes
The General Theory of Employment, Interest and Money

Chapter 2
The Postulates of the Classical Economics

MOST treatises on the theory of value and production are primarily concerned with the distribution of a *given* volume of employed resources between different uses and with the conditions which, assuming the employment of this quantity of resources, ~~determine~~ their relative rewards and the relative values of their products.[1]

The question, also, of the volume of the *available* resources, in the sense of the size of the employable population, the extent of natural wealth and the accumulated capital equipment, has often been treated descriptively. But the pure theory of what determines *the actual employment* of the available resources has seldom been examined in great detail. To say that it has not been examined at all would, of course, be absurd. For every discussion concerning fluctuations of employment, of which there have been many, has been concerned with it. I mean, not that the topic has been overlooked, but that the fundamental theory underlying it has been deemed so simple and obvious that it has received, at the most, a bare mention.[2]

Since people can invest instead

I

The classical theory of employment — supposedly simple and obvious — has been based. I think, on two fundamental postulates, though practically without discussion, namely:

i. The wage is equal to the marginal product of labour

That is to say, the wage of an employed person is equal to the value which would be lost if employment were to be reduced by one unit (after deducting any other costs which this reduction of output would avoid); subject, however, to the qualification that the equality may be disturbed, in accordance with certain principles, if competition and markets are imperfect.

circular effect

ii. The utility of the wage when a given volume of labour is employed is

equal to the marginal disutility of that amount of employment.

That is to say, the real wage of an employed person is that which is just sufficient (in the estimation of the employed persons themselves) to induce the volume of labour actually employed to be forthcoming; subject to the qualification that the equality for each individual unit of labour may be disturbed by combination between employable units analogous to the imperfections of competition which qualify the first postulate. Disutility must be here understood to cover every kind of reason which might lead a man, or a body of men, to withhold their labour rather than accept a wage which had to them a utility below a certain minimum.

This postulate is compatible with what may be called 'frictional' unemployment. For a realistic interpretation of it legitimately allows for various inexactnesses of adjustment which stand in the way of continuous full employment: for example, unemployment due to a temporary want of balance between the relative quantities of specialised resources as a result of miscalculation or intermittent demand; or to time-lags consequent on unforeseen changes; or to the fact that the change-over from one employment to another cannot be effected without a certain delay, so that there will always exist in a non-static society a proportion of resources unemployed 'between jobs'. In addition to 'frictional' unemployment, the postulate is also compatible with 'voluntary' unemployment due to the refusal or inability of a unit of labour, as a result of legislation or social practices or of combination for collective bargaining or of slow response to change or of mere human obstinacy, to accept a reward corresponding to the value of the product attributable to its marginal productivity. But these two categories of 'frictional' unemployment and 'voluntary' unemployment are comprehensive. The classical postulates do not admit of the possibility of the third category, which I shall define below as 'involuntary' unemployment.

Subject to these qualifications, the volume of employed resources is duly determined, according to the classical theory, by the two postulates. The first gives us the demand schedule for employment, the second gives us the supply schedule; and the amount of employment is fixed at the point where the utility of the marginal product balances the disutility of the marginal employment.

It would follow from this that there are only four possible means of increasing employment:

(*a*) An improvement in organisation or in foresight which diminishes 'frictional' unemployment;

(*b*) a decrease in the marginal disutility of labour, as expressed by the real wage for which. additional labour is available, so as to diminish 'voluntary' unemployment;

(*c*) an increase in the marginal physical productivity of labour in the wage-goods industries (to use Professor Pigou's convenient term for goods upon the price of which the utility of the money-wage depends);

(*d*) an increase in the price of non-wage-goods compared with, the price of wage-goods, associated with a shift in the expenditure of non-wage-earners from wage-goods to non-wage-goods.

This, to the best of my understanding, is the stance of Professor Pigou's *Theory of Unemployment* — the only detailed account of the classical theory of employment which exists.[3]

II

Is it true that the above categories are comprehensive in view of the fact that the population generally is seldom doing as much work as it would like to do on the basis of the current wage? For, admittedly, more labour would, as a rule, be forthcoming at the existing money-wage if it were demanded.[4] The classical school reconcile this phenomenon with their second postulate by arguing that, while the demand for labour at the existing money-wage may be satisfied before everyone willing to work at this wage is employed, this situation is due to an open or tacit agreement amongst workers not to work for less, and that if labour as a whole would agree to a reduction of money-wages more employment would be forthcoming. If this is the case, such unemployment, though apparently involuntary, is not strictly so, and ought to be included under the above category of 'voluntary' unemployment due to the effects of collective bargaining, etc.

This calls for two observations, the first of which relates to the actual attitude of workers towards real wages and money-wages respectively and is not theoretically fundamental, but the second of which is fundamental.

Let us assume, for the moment, that labour is not prepared to work for a lower money-wage and that a reduction in the existing level of money-wages would lead, through strikes or otherwise, to a withdrawal from the labour market of labour which is now employed. Does it follow from this that the existing level of real wages accurately measures the marginal disutility of labour? Not necessarily. For, although a reduction in the existing money-wage would lead to a withdrawal of labour, it does not follow that a fall in the value of the existing money-wage in terms of wage-goods would do so, if it were due to a rise in the price of the latter. In other words, it may be the case that within a certain range the demand of labour is for a minimum money-wage and not for a minimum real wage. The classical school have tacitly assumed that this would involve no significant change in their theory. But this is not so. For if the supply of labour is not a function of real wages as its sole variable, their argument breaks down entirely and leaves the question of what the actual employment will be quite indeterminate.[5] They do not seem to have realised that, unless the supply of labour is a function of real wages alone, their supply curve for labour will shift bodily with every movement of prices. Thus their method is tied up with their very special assumptions, and cannot be adapted to deal with the more general case.

Now ordinary experience tells us, beyond doubt, that a situation where labour stipulates (within limits) for a money-wage rather than a real wage, so far from being a mere possibility, is the normal case. Whilst workers will usually resist a reduction of money-wages, it is not their practice to withdraw their labour whenever there is a rise in the price of wage-goods. It is sometimes said that it would be illogical for labour to resist a reduction of money-wages but not to resist a reduction of real wages. For reasons given below (section III), this might not be so illogical as it appears at first; and, as we shall see later, fortunately so. But, whether logical or illogical, experience shows that this is how labour in fact behaves.

Moreover, the contention that the unemployment which characterises a depression is due to a refusal by labour to accept a reduction of money-wages is not clearly supported by the facts. It is not very plausible to assert that unemployment in the United States in 1932 was due either to labour obstinately refusing to accept a reduction of money-wages or to its obstinately demanding a real wage beyond what the productivity of the economic machine was capable of furnishing. Wide variations are experienced in the volume of employment without any apparent change either in the minimum real demands of labour or in its productivity. Labour is not more truculent in the depression than in the boom — far from it. Nor is its physical productivity less. These facts from experience are a *prima facie* ground for questioning the adequacy of the classical analysis.

It would be interesting to see the results of a statistical enquiry into the actual relationship between changes in money-wages and changes in real wages. In the case of a change peculiar to a particular industry one would expect the change in real wages to be in the same direction as the change in money-wages. But in the case of changes in the general level of wages, it will be found, I think, that the change in real wages associated with a change in money-wages, so far from being usually in the same direction, is almost always in the opposite direction. When money-wages are rising, that is to say, it will be found that real wages are falling; and when money-wages are falling, real wages are rising. This is because, in the short period, falling money-wages and rising real wages are each, for independent reasons, likely to accompany decreasing employment; labour being readier to accept wage-cuts when employment is falling off, yet real wages inevitably rising in the same circumstances on account of the increasing marginal return to a given capital equipment when output is diminished.

If, indeed, it were true that the existing real wage is a minimum below which more labour than is now employed will not be forthcoming in any circumstances, involuntary unemployment, apart from frictional unemployment, would be non-existent. But to suppose that this is invariably the case would be absurd. For more labour than is at present employed is usually available at the existing money-wage, even though the price of wage-goods is rising and, consequently, the real wage falling. If this is true, the wage-goods equivalent of the existing money-wage is not an accurate indication of the marginal disutility of labour, and the second postulate does not hold good.

reading fast

But there is a more fundamental objection. The second postulate flows from the idea that the real wages of labour depend on the wage bargains which labour makes with the entrepreneurs. It is admitted, of course, that the bargains are actually made in terms of money, and even that the real wages acceptable to labour are not altogether independent of what the corresponding money-wage happens to be. Nevertheless it is the money-wage thus arrived at which is held to determine the real wage. Thus the classical theory assumes that it is always open to labour to reduce its real wage by accepting a reduction in its money-wage. The postulate that there is a tendency for the real wage to come to equality with the marginal disutility of labour clearly presumes that labour itself is in a position to decide the real wage for which it works, though not the quantity of employment forthcoming at this wage.

The traditional theory maintains, in short, *that the wage bargains between the entrepreneurs and the workers determine the real wage;* so that, assuming free competition amongst employers and no restrictive combination amongst workers, the latter can, if they wish, bring their real wages into conformity with the marginal disutility of the amount of employment offered by the employers at that wage. If this is not true, then there is no longer any reason to expect a tendency towards equality between the real wage and the marginal disutility of labour.

The classical conclusions are intended, it must be remembered, to apply to the whole body of labour and do not mean merely that a single individual can get employment by accepting a cut in money-wages which his fellows refuse. They are supposed to be equally applicable to a closed system as to an open system, and are not dependent on the characteristics of an open system or on the effects of a reduction of money-wages in a single country on its foreign trade, which lie, of course, entirely outside the field of this discussion. Nor are they based on indirect effects due to a lower wages-bill in terms of money having certain reactions on the banking system and the state of credit, effects which we shall examine in detail in Chapter 19. They are based on the belief that in a closed system a reduction in the general level of money-wages will be accompanied, at any rate in the short period and subject only to minor qualifications, by some, though not always a proportionate, reduction in real wages.

Now the assumption that the general level of real wages depends on the money-wage bargains between the employers and the workers is not obviously true. Indeed it is strange that so little attempt should have been made to prove or to refute it. For it is far from being consistent with the general tenor of the classical theory, which has taught us to believe that prices are governed by marginal prime cost in terms of money and that money-wages largely govern marginal prime cost. Thus if money-wages change, one would have expected the classical school to argue that prices would change in almost the same proportion, leaving the real wage and the level of unemployment practically the same as before, any small gain or loss to labour being at the expense or profit of other elements of marginal cost which have been left unaltered.[6] They seem, however, to have been diverted from this line of thought, partly by the settled conviction that labour is in a position to determine its own real wage and partly, perhaps, by preoccupation with the idea that prices depend on the quantity of money. And the belief in the proposition that labour is always in a position to determine its own real wage, once adopted, has been maintained by its being confused with the proposition that labour is always in a position to determine what real wage shall correspond to full employment, i.e. the *maximum* quantity of employment which is compatible with a given real wage.

To sum up: there are two objections to the second postulate of the classical theory. The first relates to the actual behaviour of labour. A fall in real wages due to a rise in prices, with money-wages unaltered, does not, as a rule, cause the supply of available labour on offer at the current wage to fall below the amount actually employed prior to the rise of prices. To suppose that it does is to suppose that all those who are now unemployed though willing to work at the current wage will withdraw the offer of their labour in the event of even a small rise in the cost of living. Yet this strange supposition apparently underlies Professor Pigou's *Theory of Unemployment*,[7] and it is what all members of the orthodox school are tacitly assuming.

But the other, more fundamental, objection, which we shall develop in the ensuing chapters, flows from our disputing the assumption that the general level of real wages is directly determined by the character of the wage bargain. In assuming that the wage bargain determines the real wage the classical school have slipt in an illicit assumption. For there may be *no* method available to labour as a whole whereby it can bring the general level of money-wages into conformity with the marginal disutility of the current volume of employment. There may exist no expedient by which labour as a whole can reduce its *real* wage to a given figure by making revised *money* bargains with the entrepreneurs. This will be our contention. We shall endeavour to show that primarily it is certain other forces which determine the general level of real wages. The attempt to elucidate this problem will be one of our main themes. We shall argue that there has been a fundamental misunderstanding of how in this respect the economy in which we live actually works.

III

Though the struggle over money-wages between individuals and groups is often believed to determine the general level of real wages, it is, in fact, concerned with a different object. Since there is imperfect mobility of labour, and wages do not tend to an exact equality of net advantage in different occupations, any individual or group of individuals, who consent to a reduction of money-wages relatively to others, will suffer a *relative* reduction in real wages, which is a sufficient justification for them to resist it. On the other hand it would be impracticable to resist every reduction of real wages, due to a change in the purchasing-power of money which affects all workers alike; and in fact reductions of real wages arising in this way are not, as a rule, resisted unless they proceed to an extreme degree. Moreover, a resistance to reductions in money-wages applying to particular industries does not raise the same insuperable bar to an increase in aggregate employment which would result from a similar resistance to every reduction in real wages.

In other words, the struggle about money-wages primarily affects the *distribution* of the aggregate real wage between different labour-groups, and not its average amount per unit of employment, which depends, as we shall see, on a different set of forces. The effect of combination on the part of a group of workers is to protect their *relative* real wage. The *general* level of real wages depends on the other forces of the economic system.

Thus it is fortunate that the workers, though unconsciously, are instinctively more reasonable economists than the classical school, inasmuch as they resist reductions of money-wages, which are seldom or never of an all-round character, even though the existing real equivalent of these wages exceeds the marginal disutility of the existing employment; whereas they do not resist reductions of real wages, which are associated with increases in aggregate employment and leave relative money-wages unchanged, unless the reduction proceeds so far as to threaten a reduction of the real wage below the marginal disutility of the existing volume of employment. Every trade union will put up some resistance to a cut in money-wages, however small. But since no trade union would dream of striking on every occasion of a rise in the cost of living, they do not raise the obstacle to any increase in aggregate employment which is attributed to them by the classical school.

IV

We must now define the third category of unemployment, namely 'involuntary' unemployment in the strict sense, the possibility of which the classical theory does not admit.

Clearly we do not mean by 'involuntary' unemployment the mere existence of an unexhausted capacity to work. An eight-hour day does not constitute unemployment because it is not beyond human capacity to work ten hours. Nor should we regard as 'involuntary' unemployment the withdrawal of their labour by a body of workers because they do not choose to work for less than a certain real reward. Furthermore, it will be convenient to exclude 'frictional' unemployment from our definition of 'involuntary' unemployment. My definition is, therefore, as follows: *Men are involuntarily unemployed if, in the event of a small rise in the price of wage-goods relatively to the money-wage, both the aggregate supply of labour willing to work for the current money-wage and the aggregate demand for it at that wage would be greater than the existing volume of employment.* An alternative definition, which amounts, however, to the same thing, will be given in the next chapter (p. 26 below).

It follows from this definition that the equality of the real wage to the marginal disutility of employment presupposed by the second postulate, realistically interpreted, corresponds to the absence of 'involuntary' unemployment. This state of affairs we shall describe as 'full' employment, both 'frictional' and 'voluntary' unemployment being consistent with 'full" employment thus defined. This fits in, we shall find, with other characteristics of the classical theory, which is best regarded as a theory of distribution in conditions of full employment. So long as the classical postulates hold good, unemployment, which is in the above sense involuntary, cannot occur. Apparent unemployment must, therefore, be the result either of temporary loss of work of the 'between jobs' type or of intermittent demand for highly specialised resources or of the effect of a trade union 'closed shop' on the employment of free labour. Thus writers in the classical tradition, overlooking the special assumption underlying their theory, have been driven inevitably to the conclusion, perfectly logical on their assumption, that apparent unemployment (apart from the admitted exceptions) must be due at bottom to a refusal by the unemployed factors to accept a reward which corresponds to their marginal productivity. A classical economist may sympathise with labour in refusing to accept a cut in its money-wage, and he will admit that it may not be wise to make it to meet conditions which are temporary; but scientific integrity forces him to declare that this refusal is, nevertheless, at the bottom of the trouble.

Obviously, however, if the classical theory is only applicable to the case of full employment, it is fallacious to apply it to the problems of involuntary unemployment — if there be such a thing (and who will deny it?). The classical theorists resemble Euclidean geometers in a non-Euclidean world who, discovering that in experience straight lines apparently parallel often meet, rebuke the lines for not keeping straight as the only remedy for the unfortunate collisions which are occurring. Yet, in truth, there is no remedy except to throw over the axiom of parallels and to work out a non-Euclidean geometry. Something similar is required today in economics. We need to throw over the second postulate of the classical doctrine and to work out the behaviour of a system in which involuntary unemployment in the strict sense is possible.

V

In emphasising our point of departure from the classical system, we must not overlook an important point of agreement. For we shall maintain the first postulate as heretofore, subject only to the same qualifications as in the classical theory; and we must pause, for a moment, to consider what this involves.

It means that, with a given organisation, equipment and technique, real wages and the volume of output (and hence of employment) are uniquely correlated, so that, in general, an increase in employment can only occur to the accompaniment of a decline in the rate of real wages. Thus I am not disputing this vital fact which the classical economists have (rightly) asserted as indefeasible. In a given state of organisation, equipment and technique, the real wage earned by a unit of labour has a unique (inverse) correlation with the volume of employment. Thus *if* employment increases, then, in the short period, the reward per unit of labour in terms of wage-goods must, in general, decline and profits increase.[8] This is simply the obverse of the familiar proposition that industry is normally working subject to decreasing returns in the short period during which equipment etc. is assumed to be constant; so that the marginal product in the wage-good industries (which governs real wages) necessarily diminishes as employment is increased. So long, indeed, as this proposition holds, *any* means of increasing employment must lead at the same time to a diminution of the marginal product and hence of the rate of wages measured in terms of this product.

But when we have thrown over the second postulate, a decline in employment, although necessarily associated with labour's *receiving* a wage equal in value to a larger quantity of wage-goods, is not necessarily due to labour's *demanding* a larger quantity of wage-goods; and a willingness on the part of labour to accept lower money-wages is not necessarily a remedy for unemployment. The theory of wages in relation to employment, to which we are here leading up, cannot be fully elucidated, however, until Chapter 19 and its Appendix have been reached.

VI

↓ his wrong assertion

From the time of Say and Ricardo the classical economists have taught that supply creates its own demand; meaning by this in some significant, but not clearly defined, sense that the whole of the costs of production must necessarily be spent in the aggregate, directly or indirectly, on purchasing the product.

In J. S. Mill's *Principles of Political Economy* the doctrine is expressly set forth:

> What constitutes the means of payment for commodities is simply commodities. Each person's means of paying for the productions of other people consist of those which he himself possesses. All sellers are inevitably, and by the meaning of the word, buyers. Could we suddenly double the productive powers of the country, we should double the supply of commodities in every market; but we should, by the same stroke, double the purchasing power. Everybody would bring a double demand as well as supply; everybody would be able to buy twice as much, because every one would have twice as much to offer in exchange. [*Principles of Political Economy*, Book III, Chap. xiv. § 2.]

As a corollary of the same doctrine, it has been supposed that any individual act of abstaining from consumption necessarily leads to, and amounts to the same thing as, causing the labour and commodities thus released from supplying consumption to be invested in the production of capital wealth. The following passage from Marshall's *Pure Theory of Domestic Values*[9] illustrates the traditional approach:

> The whole of a man's income is expended in the purchase of services and of commodities. It is indeed commonly said that a man spends some portion of his income and saves another. But it is a familiar economic axiom that a man purchases labour and commodities with that portion of his income which he saves just as much as he does with that he is said to spend. He is said to spend when he seeks to obtain present enjoyment from the services and commodities which he purchases. He is said to save when he causes the labour and the commodities which he purchases to be devoted to the production of wealth from which he expects to derive the means of enjoyment in the future.

It is true that it would not be easy to quote comparable passages from Marshall's later work[10] or from Edgeworth or Professor Pigou. The doctrine is never stated today in this crude form. Nevertheless it still underlies the whole classical theory, which would collapse without it. Contemporary economists, who might hesitate to agree with Mill, do not hesitate to accept conclusions which require Mill's doctrine as their premise. The conviction, which runs, for example, through almost all Professor Pigou's work, that money makes no real difference except frictionally and that the theory of production and employment can be worked out (like Mill's) as being based on 'real' exchanges with money introduced perfunctorily in a later chapter, is the modern version of the classical tradition. Contemporary thought is still deeply steeped in the notion that if people do not spend their money in one way they will spend it in another.[11] Post-war economists seldom, indeed, succeed in maintaining this standpoint *consistently;* for their thought today is too much permeated with the contrary tendency and with facts of experience too obviously inconsistent with their former view.[12] But they have not drawn sufficiently far-reaching consequences; and have not revised their fundamental theory.

In the first instance, these conclusions may have been applied to the kind of economy in which we actually live by false analogy from some kind of non-exchange Robinson Crusoe economy, in which the income which individuals consume or retain as a result of their productive activity is, actually and exclusively, the output *in specie* of that activity. But, apart from this, the conclusion that the *costs* of output are always covered in the aggregate by the sale-proceeds resulting from demand, has great plausibility, because it is difficult to distinguish it from another, similar-looking proposition which is indubitable, namely that income derived in the aggregate by all the elements in the community concerned in a productive activity necessarily has a value exactly equal to the *value* of the output.

Similarly it is natural to suppose that the act of an individual, by which he enriches himself without apparently taking anything from anyone else, must also enrich the community as a whole; so that (as in the passage just quoted from Marshall) an act of individual saving inevitably leads to a parallel act of investment. For, once more, it is indubitable that the sum of the net increments of the wealth of individuals must be exactly equal to the aggregate net increment of the wealth of the community.

Those who think in this way are deceived, nevertheless, by an optical illusion, which makes two essentially different activities appear to be the same. They are fallaciously supposing that there is a nexus which unites decisions to abstain from present consumption with decisions to provide for future consumption; whereas the motives which determine the latter are not linked in any simple way with the motives which determine the former.

It is, then, the assumption of equality between the demand price of output as a whole and its supply price which is to be regarded as the classical theory's 'axiom of parallels'. Granted this, all the rest follows — the social advantages of private and national thrift, the traditional attitude towards the rate of interest, the classical theory of unemployment, the quantity theory of money, the unqualified advantages of *laissez-faire* in respect of foreign trade and much else which we shall have to question.

VII

At different points in this chapter we have made the classical theory to depend in succession on the assumptions:

(1) that the real wage is equal to the marginal disutility of the existing employment;

(2) that there is no such thing as involuntary unemployment in the strict sense;

(3) that supply creates its own demand in the sense that the aggregate demand price is equal to the aggregate supply price for all levels of output and employment.

These three assumptions, however, all amount to the same thing in the sense that they all stand and fall together, any one of them logically involving the other two.

Author's Footnotes

1. This is in the Ricardian tradition. For Ricardo expressly repudiated any interest in the *amount* of the national dividend, as distinct from its distribution. In this he was assessing correctly the character of his own theory. But his successors, less clear-sighted, have used the classical theory in discussions concerning the causes of wealth. *Vide* Ricardo's letter to Malthus of October 9, 1820: "Political Economy you think is an enquiry into the nature and causes of wealth — I think it should be called an enquiry into the laws which determine the division of the produce of industry amongst the classes who concur in its formation. No law can be laid down respecting quantity, but a tolerably correct one can be laid down respecting proportions. Every day I am more satisfied that the former enquiry is vain and delusive, and the latter only the true objects of the science."

2. For example, Prof. Pigou in the *Economics of Welfare* (4th ed. p. 127) writes (my italics): "Throughout this discussion, except when the contrary is expressly stated, the fact that some resources are generally unemployed against the will of the owners is ignored. *This does not affect the substance of the argument,* while it simplifies its exposition.". Thus, whilst Ricardo expressly disclaimed any attempt to deal with the amount of the national dividend as a whole, Prof. Pigou, in a book which is specifically directed to the problem of the national dividend, maintains that the same theory holds when there is some involuntary unemployment as in the case of full employment.

3. Prof. Pigou's *Theory of Unemployment* is examined in more detail in the Appendix to Chapter 19 below.

4. *Cf.* the quotation from Prof. Pigou above, p. 5, footnote.

5. This point is dealt with in detail in the Appendix to Chapter 19 below.

6. This argument would, indeed, contain, to my thinking, a large element of truth, though the complete results of a change in money-wages are more complex, as we shall show in Chapter 19 below.

7. Cf. Chapter 19, Appendix.

8. The argument runs as follows: n men are employed, the nth man adds a bushel a day to the harvest, and wages have a buying power of a bushel a day. The $n + 1$ th man, however, would only add .9 bushel a day, and employment cannot, therefore, rise to $n + 1$ men unless the price of corn rises relatively to wages until daily wages have a buying power of .9 bushel. Aggregate wages would then amount to 9/10 $(n + 1)$ bushels as compared with n bushels previously. Thus the employment of an additional man will, if it occurs, necessarily involve a transfer of income from those previously in work to the entrepreneurs.

9. p. 34.

10. Mr. J. A. Hobson, after quoting in his *Physiology of Industry* (p. 102) the above passage from Mill, points out that Marshall commented as follows on this passage as early as his *Economics of Industry,* p. 154. "But though men have the power to purchase, they may not choose to use it." "But", Mr Hobson continues, "he fails to grasp the critical importance of this fact, and appears to limit its action to periods of 'crisis'." This has remained fair comment, I think, in the light of Marshall's later work.

11. *Cf.* Alfred and Mary Marshall, *Economics of Industry,* p. 17: "It is not good for trade to have dresses made of material which wears out quickly. For if people did not spend their means on buying new dresses they would spend them on giving employment to labour in some other way." The reader will notice that I am again quoting from the earlier Marshall. The Marshall of the *Principles* had become sufficiently doubtful to be very cautious and evasive. But the old ideas were never repudiated or rooted out of the basic assumptions of his thought.

12. It is this distinction of Prof. Robbins that he, almost alone, continues to maintain a consistent scheme of thought, his practical recommendations belonging to the same system as his theory.

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John Maynard Keynes
The General Theory of Employment, Interest and Money

Chapter 3. The Principle of Effective Demand

I

WE need, to start with, a few terms which will be defined precisely later. In a given state of technique, resources and costs, the employment of a given volume of labour by an entrepreneur involves him in two kinds of expense: first of all, the amounts which he pays out to the factors of production (exclusive of other entrepreneurs) for their current services, which we shall call the *factor cost* of the employment in question; and secondly, the amounts which he pays out to other entrepreneurs for what he has to purchase from them together with the sacrifice which he incurs by employing the equipment instead of leaving it idle, which we shall call the *user cost* of the employment in question.[1] The excess of the value of the resulting output over the sum of its factor cost and its user cost is the profit or, it we shall call it, the *income* of the entrepreneur. The factor cost is, of course, the same thing, looked at from the point of view of the entrepreneur, as what the factors of production regard as their income. Thus the factor cost and the entrepreneur's profit make up, between them, what we shall define as the *total income* resulting from the employment given by the entrepreneur. The entrepreneur's profit thus defined is, as it should be, the quantity which he endeavours to maximise when he is deciding what amount, of employment to offer. It is sometimes convenient, when we are looking at it from the entrepreneur's standpoint, to call the aggregate income (*i.e.* factor cost *plus* profit) resulting from a given amount of employment the *proceeds* of that employment. On the other hand, the aggregate supply price[2] of the output of a given amount of employment is the expectation of proceeds which will just make it worth the while of the entrepreneurs to give that employment.[3]

It follows that in a given situation of technique, resources and factor cost per unit of employment, the amount of employment, both in each individual firm and industry and in the aggregate, depends on the amount of the proceeds which the entrepreneurs expect to receive from the corresponding output.[4] For entrepreneurs will endeavour to fix the amount of employment at the level which they expect to maximise the excess of the proceeds over the factor cost.

Let Z be the aggregate supply price of the output from employing N men, the relationship between Z and N being written $Z = \varphi(N)$, which can be called the *Aggregate Supply Function.*[5] Similarly, let D be the proceeds which entrepreneurs expect to receive from the employment of N men, the relationship between D and N being written $D = f(N)$, which can be called the *Aggregate Demand Function.*

does hap math

Now if for a given value of N the expected proceeds are greater than the aggregate supply price, *i.e.* if D is greater than Z, there will be an incentive to entrepreneurs to increase employment beyond N and, if necessary, to raise costs by competing with one another for the factors of production, up to the value of N for which Z has become equal to D. Thus the volume of employment is given by the point of intersection between the aggregate demand function and the aggregate supply function; for it is at this point that the entrepreneurs' expectation of profits will be maximised. The value of D at the point of the aggregate demand function, where it is intersected by the aggregate supply function, will be called *the effective demand.* Since this is the substance of the General Theory of Employment, which it will be our object to expound, the succeeding chapters will be largely occupied with examining the various factors upon which these two functions depend.

The classical doctrine, on the other hand, which used to be expressed categorically in the statement that "Supply creates its own Demand" and continues to underlie all orthodox economic theory, involves a special assumption as to the relationship between these two functions. For "Supply creates its own Demand" must mean that f(N) and φ(N) are equal for all values of N, *i.e.* for all levels of output and employment; and that when there is an increase in Z(= f(N)) corresponding to an increase in N, D(=f(N)) necessarily increases by the same amount as Z. The classical theory assumes, in other words, that the aggregate demand price (or proceeds) always accommodates itself to the aggregate supply price; so that, whatever the value of N may be, the proceeds D assume a value equal to the aggregate supply price Z which corresponds to N. That is to say, effective demand, instead of having a unique equilibrium value, is an infinite range of values all equally admissible; and the amount of employment is indeterminate except in so far as the marginal disutility of labour sets an upper limit.

If this were true, competition between entrepreneurs would always lead to an expansion of employment up to the point at which the supply of output as a whole ceases to be elastic, i.e. where a further increase in the value of the effective demand will no longer be accompanied by any increase in output. Evidently this amounts to the same thing as full employment. In the previous chapter we have given a definition of full employment in terms of the behaviour of labour. An alternative, though equivalent, criterion is that at which we have now arrived, namely a situation, in which aggregate employment is inelastic in response to an increase in the effective demand for its output. Thus Say's law, that the aggregate demand price of output as a whole is equal to its aggregate supply price for all volumes of output, is equivalent to the proposition that there is no obstacle to full employment. If, however, this is not the true law relating the aggregate demand and supply functions, there is a vitally important chapter of economic theory which remains to be written and without which all discussions concerning the volume of aggregate employment are futile.

multiplier?

II

A brief summary of the theory of employment to be worked out in the course of the following chapters may, perhaps, help the reader at this stage, even though it may not be fully intelligible. The terms involved will be more carefully defined in due course. In this summary we shall assume that the money-wage and other factor costs are constant per unit of labour employed. But this simplification, with which we shall dispense later, is introduced solely to facilitate the exposition. The essential character of the argument is precisely the same whether or not money-wages, etc., are liable to change.

The outline of our theory can be expressed as follows. When employment increases aggregate real income is increased. The psychology of the community is such that when aggregate real income is increased aggregate consumption is increased, but not by so much as income. Hence employers would make a loss if the whole of the increased employment were to be devoted to satisfying the increased demand for immediate consumption. Thus, to justify any given amount of employment there must be an amount of current investment sufficient to absorb the excess of total output over what the community chooses to consume when employment is at the given level. For unless there is this amount of investment, the receipts of the entrepreneurs will be less than is required to induce them to offer the given amount of employment. It follows, therefore, that, given what we shall call the community's propensity to consume, the equilibrium level of employment, i.e. the level at which there is no inducement to employers as a whole either to expand or to contract employment, will depend on the amount of current investment. The amount of current investment will depend, in turn, on what we shall call the inducement to invest; and the inducement to invest will be found to depend on the relation between the schedule of the marginal efficiency of capital and the complex of rates of interest on loans of various maturities and risks.

need math/ Charts to actually evaluate

Thus, given the propensity to consume and the rate of new investment, there will be only one level of employment consistent with equilibrium; since any other level will lead to inequality between the aggregate supply price of output as a whole and its aggregate demand price. This level cannot be *greater* than full employment, i.e. the real wage cannot be less than the marginal disutility of labour. But there is no reason in general for expecting it to be *equal* to full employment. The effective demand associated with full employment is a special case, only realised when the propensity to consume and the inducement to invest stand in a particular relationship to one another. This particular relationship, which corresponds to the assumptions of the classical theory, is in a sense an optimum relationship. But it can only exist when, by accident or design, current investment provides an amount of demand just equal to the excess of the aggregate supply price of the output resulting from full employment over what the community will choose to spend on consumption when it is fully employed.

This theory can be summed up in the following propositions:

(1) In a given situation of technique, resources and costs, income (both money-income and real income) depends on the volume of employment N.

(2) The relationship between the community's income and what it can be expected to spend on consumption, designated by D_1, will depend on the psychological characteristic of the community, which we shall call its *propensity to consume*. That is to say, consumption will depend on the level of aggregate income and, therefore, on the level of employment N, except when there is some change in the propensity to consume.

hard to know what came befor

(3) The amount of labour N which the entrepreneurs decide to employ depends on the sum (D) of two quantities, namely D_1, the amount which the community is expected to spend on consumption, and D_2, the amount which it is expected to devote to new investment. D is what we have called above the *effective demand*. (C+I)

(4) Since $D_1 + D_2 = D = \varphi(N)$, where φ is the aggregate supply function, and since, as we have seen in (2) above, D_1 is a function of N, which we may write $\chi(N)$, depending on the propensity to consume, it follows that $\varphi(N) - \chi(N) = D_2$.

(5) Hence the volume of employment in equilibrium depends on (i) the aggregate supply function, φ, (ii) the propensity to consume, χ, and (iii) the volume of investment, D_2. This is the essence of the General Theory of Employment.

(6) For every value of N there is a corresponding marginal productivity of labour in the wage-goods industries; and it is this which determines the real wage. (5) is, therefore, subject to the condition that N cannot *exceed* the value which reduces the real wage to equality with the marginal disutility of labour. This means that not all changes in D are

compatible with our temporary assumption that money-wages are constant. Thus it will be essential to a full statement of our theory to dispense with this assumption.

(7) On the classical theory, according to which $D = \varphi(N)$ for all values of N, the volume of employment is in neutral equilibrium for all values of N less than its maximum value; so that the forces of competition between entrepreneurs may be expected to push it to this maximum value. Only at this point, on the classical theory, can there be stable equilibrium.

(8) *When employment increases,* D_1 *will increase, but not by so much as* D; since when our income increases our consumption increases also, but not by so much. The key to our practical problem is to be found in this psychological law. For it follows from this that the greater the volume of employment the greater will be the gap between the aggregate supply price (Z) of the corresponding output and the sum (D_1) which the entrepreneurs can expect to get back out of the expenditure of consumers. Hence, if there is no change in the propensity to consume, employment cannot increase, unless at the same time D_2 is increasing so as to fill the increasing gap between Z and D_1. Thus — except on the special assumptions of the classical theory according to which there is some force in operation which, when employment increases, always causes D_2 to increase sufficiently to fill the widening gap between Z and D_1 — the economic system may find itself in stable equilibrium with N at a level below full employment, namely at the level given by the intersection of the aggregate demand function with the aggregate supply function.

Investments ↑

Thus the volume of employment is not determined by the marginal disutility of labour measured in terms of real wages, except in so far as the supply of labour available at a given real wage sets a *maximum* level to employment. The propensity to consume and the rate of new investment determine between them the volume of employment, and the volume of employment is uniquely related to a given level of real wages — not the other way round. If the propensity to consume and the rate of new investment result in a deficient effective demand, the actual level of employment will fall short of the supply of labour potentially available at the existing real wage, and the equilibrium real wage will be *greater* than the marginal disutility of the equilibrium level of employment.

This analysis supplies us with an explanation of the paradox of poverty in the midst of plenty. For the mere existence of an insufficiency of effective demand may, and often will, bring the increase of employment to a standstill *before* a level of full employment has been reached. The insufficiency of effective demand will inhibit the process of production in spite of the fact that the marginal product of labour still exceeds in value the marginal disutility of employment.

Moreover the richer the community, the wider will tend to be the gap between its actual and its potential production; and therefore the more obvious and outrageous the defects of the economic system. For a poor community will be prone to consume by far the greater part of its output, so that a very modest measure of investment will be sufficient to provide full employment; whereas a wealthy community will have to discover much ampler opportunities for investment if the saving propensities of its wealthier members are to be compatible with the employment of its poorer members. If in a potentially wealthy community the inducement to invest is weak, then, in spite of its potential wealth, the working of the principle of effective demand will compel it to reduce its actual output, until, in spite of its potential wealth, it has become so poor that its surplus over its consumption is sufficiently diminished to correspond to the weakness of the inducement to invest.

But worse still. Not only is the marginal propensity to consume[6] weaker in a wealthy community, but, owing to its accumulation of capital being already larger, the opportunities for further investment are less attractive unless the rate of interest falls at a sufficiently rapid rate; which brings us to the theory of the rate of interest and to the reasons why it does not automatically fall to the appropriate level, which will occupy Book IV.

Thus the analysis of the Propensity to Consume, the definition of the Marginal Efficiency of Capital and the theory of the Rate of Interest are the three main gaps in our existing knowledge which it will be necessary to fill. When this has been accomplished, we shall find that the Theory of Prices falls into its proper place as a matter which is subsidiary to our general theory. We shall discover, however, that Money plays an essential part in our theory of the Rate of Interest; and we shall attempt to disentangle the peculiar characteristics of Money which distinguish it from other things.

III

The idea that we can safely neglect the aggregate demand function is fundamental to the Ricardian economics, which underlie what we have been taught for more than a century. Malthus, indeed, had vehemently opposed Ricardo's doctrine that it was impossible for effective demand to be deficient; but vainly. For, since Malthus was unable to explain clearly (apart from an appeal to the facts of common observation) how and why effective demand could be deficient or excessive, he failed to furnish an alternative construction; and Ricardo conquered England as completely as the Holy Inquisition conquered Spain. Not only was his theory accepted by the city, by statesmen and by the academic world. But controversy ceased; the other point of view completely disappeared; it ceased to be discussed. The great puzzle of Effective Demand with which Malthus had wrestled vanished from economic literature. You will not find it mentioned even once in the whole works of Marshall, Edgeworth and Professor Pigou, from whose hands the classical theory has received its most mature embodiment. It could only live on furtively, below the surface, in the underworlds of Karl Marx, Silvio Gesell or Major Douglas.

The completeness of the Ricardian victory is something of a curiosity and a mystery. It must have been due to a complex of suitabilities in the doctrine to the environment into which it was projected. That it reached conclusions quite different from what the ordinary uninstructed person would expect, added, I suppose, to its intellectual prestige. That its teaching, translated into practice, was austere and often unpalatable, lent it virtue. That it was adapted to carry a vast and consistent logical superstructure, gave it beauty. That it could explain much social injustice and apparent cruelty as an inevitable incident in the scheme of progress, and the attempt to change such things as likely on the whole to do more harm than good, commanded it to authority. That it afforded a measure of justification to the free activities of the individual capitalist, attracted to it the support of the dominant social force behind authority.

But although the doctrine itself has remained unquestioned by orthodox economists up to a late date, its signal failure for purposes of scientific prediction has greatly impaired, in the course of time, the prestige of its practitioners. For professional economists, after Malthus, were apparently unmoved by the lack of correspondence between the results of their theory and the facts of observation;— a discrepancy which the ordinary man has not failed to observe, with the result of his growing unwillingness to accord to economists that measure of respect which he gives to other groups of scientists whose theoretical results are confirmed by observation when they are applied to the facts.

The celebrated *optimism* of traditional economic theory, which has led to economists being looked upon as Candides, who, having left this world for the cultivation of their gardens, teach that all is for the best in the best of all possible worlds provided we will let well alone, is also to be traced, I think, to their having neglected to take account of the drag on prosperity which can be exercised by an insufficiency of effective demand. For there would obviously be a natural tendency towards the optimum employment of resources in a Society which was functioning after the manner of the classical postulates. It may well be that the classical theory represents the way in which we should like our Economy to behave. But to assume that it actually does so is to assume our difficulties away.

Author's Footnotes

1. A precise definition of *user cost* will be given in Chapter 6.

2. Not to be confused (*vide infra*) with the supply price of a unit of output in the ordinary sense of this term.

3. The reader will observe that I am deducting the user cost both from the *proceeds* and from the *aggregate supply price* of a given volume of output, so that both these terms are to be interpreted *net* of user cost; whereas the aggregate sums paid by the purchasers are, of course, *gross* of user cost. The reasons why this is convenient will be given in Chapter 6. The essential point is that the aggregate proceeds and aggregate supply price net of user cost can be defined uniquely and unambiguously; whereas, since user cost is obviously dependent both on the degree of integration of industry and on the extent to which entrepreneurs buy from one another, there can be no definition of the aggregate sums paid by purchasers, *inclusive* of user cost, which is independent of these factors. There is a similar difficulty even in defining supply price in the ordinary sense for an individual producer; and in the case of the aggregate supply price of *output as a whole* serious difficulties of duplication are involved, which have not always been faced. If the term is to be interpreted gross of user cost, they can only be overcome by making special assumptions relating to the integration of entrepreneurs in groups according as they produce consumption-goods or capital-goods which are obscure and complicated in themselves and do not correspond to the facts. If, however, aggregate supply price is defined as above *net* of user cost, thew difficulties do not arise. The reader is advised, however, to await the fuller discussion in Chapter 6 and its appendix.

4. An entrepreneur, who has to reach a practical decision as to his scale of production, does not, of course, entertain a single undoubting expectation of what the sale-proceeds of a given output will be, but several hypothetical expectations held with varying degrees of probability and definiteness. By his expectation of proceeds I mean, therefore, that expectation of proceeds which, if it were held with certainty, would lead to the same behaviour as does the bundle of vague and more various possibilities which actually makes up his state of expectation when he reaches his decision.

5. In Chapter 20 a function closely related to the above will be called the employment function.

6. Defined in Chapter 10, below.

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Chapter 18. The General Theory of Employment Re-Stated

I

WE have now reached a point where we can gather together the threads of our argument. To begin with, it may be useful to make clear which elements in the economic system we usually take as given, which are the independent variables of our system and which are the dependent variables.

We take as given the existing skill and quantity of available labour, the existing quality and quantity of available equipment, the existing technique, the degree of competition, the tastes and habits of the consumer, the disutility of different intensifies of labour and of the activities of supervision and organisation, as well as the social structure including the forces, other than our variables set forth below, which determine the distribution of the national income. This does not mean that we assume these factors to be constant; but merely that, in this place and context, we are not considering or taking into account the effects and consequences of changes in them.

Our independent variables are, in the first instance, the propensity to consume, the schedule of the marginal efficiency of capital and the rate of interest, though, as we have already seen, these are capable of further analysis.

Our dependent variables are the volume of employment and the national income (or national dividend) measured in wage-units.

The factors, which we have taken as given, influence our independent variables, but do not completely determine them. For example, the schedule of the marginal efficiency of capital depends partly on the existing quantity of equipment which is one of the given factors, but partly on the state of long-term expectation which cannot be inferred from the given factors. But there are certain other elements which the given factors determine so completely that we can treat these derivatives as being themselves given. For example, the given factors allow us to infer what level of national income measured in terms of the wage-unit will correspond to any given level of employment; so that, within the economic framework which we take as given, the national income depends on the volume of employment, *i.e.* on the quantity of effort currently devoted to production, in the sense that there is a unique correlation between the two.[1] Furthermore, they allow us to infer the shape of the aggregate supply functions, which embody the *physical* conditions of supply, for different types of products; — that is to say, the quantity of employment which will be devoted to production corresponding to any given level of effective demand measured in terms of wage-units. Finally, they furnish us with the supply function of labour (or effort); so that they tell us *inter alia* at what point the employment function[2] for labour as a whole will cease to be elastic.

The schedule of the marginal efficiency of capital depends, however, partly on the given factors and partly on the prospective yield of capital-assets of different kinds; whilst the rate of interest depends partly on the state of liquidity-preference (*i.e.* on the liquidity function) and partly on the quantity of money measured in terms of wage-units. Thus we can sometimes regard our ultimate independent variables as consisting of (1) the three fundamental psychological factors, namely, the psychological propensity to consume, the psychological attitude to liquidity and the psychological expectation of future yield from capital-assets, (2) the wage-unit as determined by the bargains reached between employers and employed, and (3) the quantity of money as determined by the action of the central bank; so that, if we take as given the factors specified above, these variables determine the national income (or dividend) and the quantity of employment. But these again would be capable of being subjected to further analysis, and are not, so to speak, our ultimate atomic independent elements.

The division of the determinants of the economic system into the two groups of given factors and independent variables is, of course, quite arbitrary from any absolute standpoint. The division must be made entirely on the basis of experience, so as to correspond on the one hand to the factors in which the changes seem to be so slow or so little relevant as to have only a small and comparatively negligible short-term influence on our *quaesitum;* and on the other hand to those factors in which the changes are found in practice to exercise a dominant influence on our *quaesitum.* Our present object is to discover what determines at any time the national income of a given economic system and (which is almost the same thing) the amount of its employment; which means in a study so complex as economics, in which we cannot hope to make completely accurate generalisations, the factors whose changes *mainly* determine our *quaesitum.* Our final task might be to select those variables which can be deliberately controlled or managed by central authority in the kind of system in which we actually live.

II

Let us now attempt to summarise the argument of the previous chapters; taking the factors in the reverse order to that in which we have introduced them.

There will be an inducement to push the rate of new investment to the point which forces the supply-price of each type of capital-asset to a figure which, taken in conjunction with its prospective yield, brings the marginal efficiency of capital in general to approximate equality with the rate of interest. That is to say, the physical conditions of supply in the capital-goods industries, the state of confidence concerning the prospective yield, the psychological attitude to liquidity and the quantity of money (preferably calculated in terms of wage-units) determine, between them, the rate of new investment.

But an increase (or decrease) in the rate of investment will have to carry with it an increase (or decrease) in the rate of consumption; because the behaviour of the public is, in general, of such a character that they are only willing to widen (or narrow) the gap between their income and their consumption if their income is being increased (or diminished). That is to say, changes in the rate of consumption are, in general, *in the same direction* (though smaller in amount) as changes in the rate of income. The relation between the increment of consumption which has to accompany a given increment of saving is given by the marginal propensity to consume. The ratio, thus determined, between an increment of investment and the corresponding increment of aggregate income, both measured in wage-units, is given by the investment multiplier.

Finally, if we assume (as a first approximation) that the employment multiplier is equal to the investment multiplier, we can, by applying the multiplier to the increment (or decrement) in the rate of investment brought about by the factors first described, infer the increment of employment.

An increment (or decrement) of employment is liable, however, to raise (or lower) the schedule of liquidity-preference; there being three ways in which it will tend to increase the demand for money, inasmuch as the value of output will rise when employment increases even if the wage-unit and prices (in terms of the wage-unit) are unchanged, but, in addition, the wage-unit itself will tend to rise as employment improves, and the increase in output will be accompanied by a rise of prices (in terms of the wage-unit) owing to increasing cost in the short period.

Thus the position of equilibrium will be influenced by these repercussions; and there are other repercussions also. Moreover, there is not one of the above factors which is not liable to change without much warning, and sometimes substantially. Hence the extreme complexity of the actual course of events. Nevertheless, these seem to be the factors which it is useful and convenient to isolate. If we examine any actual problem along the lines of the above schematism, we shall find it more manageable; and our practical intuition (which can take account of a more detailed complex of facts than can be treated on general principles) will be offered a less intractable material upon which to work.

III

The above is a summary of the General Theory. But the actual phenomena of the economic system are also coloured by certain special characteristics of the propensity to consume, the schedule of the marginal efficiency of capital and the rate of interest, about which we can safely generalise from experience, but which are not logically necessary.

In particular, it is an outstanding characteristic of the economic system in which we live that, whilst it is subject to severe fluctuations in respect of output and employment, it is not violently unstable. Indeed it seems capable of remaining in a chronic condition of sub-normal activity for a considerable period without any marked tendency either towards recovery or towards complete collapse. Moreover, the evidence indicates that full, or even approximately full, employment is of rare and short-lived occurrence. Fluctuations may start briskly but seem to wear themselves out before they have proceeded to great extremes, and an intermediate situation which is neither desperate nor satisfactory is our normal lot. It is upon the fact that fluctuations tend to wear themselves out before proceeding to extremes and eventually to reverse themselves, that the theory of business *cycles* having a regular phase has been founded. The same thing is true of prices, which, in response to an initiating cause of disturbance, seem to be able to find a level at which they can remain, for the time being, moderately stable.

Now, since these facts of experience do not follow of logical necessity, one must suppose that the environment and the psychological propensities of the modern world must be of such a character as to produce these results. It is, therefore, useful to consider what hypothetical psychological propensities would lead to a stable system; and, then, whether these propensities can be plausibly ascribed, on our general knowledge of contemporary human nature, to the world in which we live.

The conditions of stability which the foregoing analysis suggests to us as capable of explaining the observed results are the following:

(i) The marginal propensity to consume is such that, when the output of a given community increases (or decreases) because more (or less) employment is being applied to its capital equipment, the multiplier relating the two is greater than unity but not very large.

(ii) When there is a change in the prospective yield of capital or in the rate of interest, the schedule of the marginal efficiency of capital will be such that the change in new investment will not be in great disproportion to the change in the former ; *i.e.* moderate changes in the prospective yield of capital or in the rate of interest will not be associated with very great changes in the rate of investment.

(iii) When there is a change in employment, money-wages tend to change in the same direction as, but not in great disproportion to, the change in employment; *i.e.* moderate changes in employment are not associated with very great chances in money-wages. This is a condition of the stability of prices rather than of employment.

(iv) We may add a fourth condition, which provides not so much for the stability of the system as for the tendency of a fluctuation in one direction to reverse itself in due course; namely, that a rate of investment, higher (or lower) than prevailed formerly, begins to react unfavourably (or favourably) on the marginal efficiency of capital if it is continued for a period which, measured in years, is not very large.

(i) Our first condition of stability, namely, that the multiplier, whilst greater than unity, is not very great, is highly plausible as a psychological characteristic of human nature. As real income increases, both the pressure of present needs diminishes and the margin over the established standard of life is increased; and as real income diminishes the opposite is true. Thus it is natural — at any rate on the average of the community — that current consumption should be expanded when employment increases) but by less than the full increment of real income; and that it should be diminished when employment diminishes, but by less than the full decrement of real income. Moreover, what is true of the average of individuals is likely to be also true of governments especially in an age when a progressive increase of unemployment will usually force the State to provide relief out of borrowed funds.

But whether or not this psychological law strikes the reader as plausible *a priori,* it is certain that experience would be extremely different from what it is if the law did not hold. For in that case an increase of investment, however small, would set moving a cumulative increase of effective demand until a position of full employment had been reached; while a decrease of investment would set moving a cumulative decrease of effective demand until no one at all was employed. Yet experience shows that we are generally in an intermediate position. It is not impossible that there may be a range within which instability does in fact prevail. But, if so, it is probably a narrow one, outside of which in either direction our psychological law must unquestionably hold good. Furthermore, it is also evident that the multiplier, though exceeding unity, is not, in normal circumstances, enormously large. For, if it were, a given change in the rate of investment would involve a great change (limited only by full or zero employment) in the rate of consumption.

(ii) Whilst our first condition provides that a moderate change in the rate of investment will not involve an indefinitely great change in the demand for consumption-goods our second condition provides that a moderate change in the prospective yield of capital-assets or in the rate of interest will not involve an indefinitely great change in the rate of investment. This is likely to be the case owing to the increasing cost of producing a greatly enlarged output from the existing equipment. If, indeed, we start from a position where there are very large surplus resources for the production of capital-assets, there may be considerable instability within a certain range; but this will cease to hold good as soon as the surplus is being largely utilised. Moreover, this condition sets a limit to the instability resulting from rapid changes in the prospective yield of capital-assets due to sharp fluctuations in business psychology or to epoch-making inventions — though more, perhaps, in the upward than in the downward direction.

(iii) Our third condition accords with our experience of human nature. For although the struggle for money-wages is, as we have pointed out above, essentially a struggle to maintain a high *relative* wage, this struggle is likely, as employment increases, to be intensified in each individual case both because the bargaining position of the worker is improved and because the diminished marginal utility of his wage and his improved financial margin make him readier to run risks. Yet, all the same, these motives will operate within limits, and workers will not seek a much greater money-wage when employment improves or allow a very great reduction rather than suffer any unemployment at all.

But here again, whether or not this conclusion is plausible *a priori,* experience shows that some such psychological law must actually hold. For if competition between unemployed workers always led to a very great reduction of the money-wage, there would be a violent instability in the price-level. Moreover, there might be no position of stable equilibrium except in conditions consistent with full employment; since the wage-unit might have to fall without limit until it reached a point where the effect of the abundance of money in terms of the wage-unit on the rate of interest was sufficient to restore a level of full employment. At no other point could there be a resting-place.[3]

(iv) Our fourth condition, which is a condition not so much of stability as of alternate recession and recovery, is merely based on the presumption that capital-assets are of various ages, wear out with time and are not all very long-lived; so that if the rate of investment falls below a certain minimum level, it is merely a question of time (failing large fluctuations in other factors) before the marginal efficiency of capital rises sufficiently to bring about a recovery of investment above this minimum. And similarly, of course, if investment rises to a higher figure than formerly, it is only a question of time before the marginal efficiency of capital falls sufficiently to bring about a recession unless there are compensating changes in other factors.

For this reason, even those degrees of recovery and recession, which can occur within the limitations set by our other conditions of stability, will be likely, if they persist for a sufficient length of time and are not interfered with by changes in the other factors, to cause a reverse movement in the opposite direction, until the same forces as before again reverse the direction.

Thus our four conditions together are adequate to explain the outstanding features of our actual experience; — namely, that we oscillate, avoiding the gravest extremes of fluctuation in employment and in prices in both directions, round an intermediate position appreciably below full employment and appreciably above the minimum employment a decline below which would endanger life.

But we must not conclude that the mean position thus determined by "natural" tendencies, namely, by those tendencies which are likely to persist, failing measures expressly designed to correct them, is, therefore, established by laws of necessity. The unimpeded rule of the above conditions is a fact of observation concerning the world as it is or has been, and not a necessary principle which cannot be changed.

Author's Footnotes

1. We are ignoring at this stage certain complications which arise when the employment functions of different products have different curvatures within the relevant range of employment. See Chapter 20 below.

2. Defined in Chapter 20 below.

3. The effects of changes in the wage-unit will be considered in detail in Chapter 19.

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Book V
Money-Wages and Prices

Chapter 19. Changes in Money-Wages

I

IT would have been an advantage if the effects of a change in money-wages could have been discussed in an earlier chapter. For the Classical Theory has been accustomed to rest the supposedly self-adjusting character of the economic system on an assumed fluidity of money-wages; and, when there is rigidity, to lay on this rigidity the blame of maladjustment.

It was not possible, however, to discuss this matter fully until our own theory had been developed. For the consequences of a change in money-wages are complicated. A reduction in money-wages is quite capable in certain circumstances of affording a stimulus to output, as the classical theory supposes. My difference from this theory is primarily a difference of analysis; so that it could not be set forth clearly until the reader was acquainted with my own method.

The generally accepted explanation is, as I understand it, quite a simple one. It does not depend on roundabout repercussions, such as we shall discuss below. The argument simply is that a reduction in money-wages will *cet. par.* stimulate demand by diminishing the price of the finished product, and will therefore increase output and employment up to the point where the reduction which labour has agreed to accept in its money-wages is just offset by the diminishing marginal efficiency of labour as output (from a given equipment) is increased.

In its crudest form, this is tantamount to assuming that the reduction in money-wages will leave demand unaffected. There may be some economists who would maintain that there is no reason why demand should be affected, arguing that aggregate demand depends on the quantity of money multiplied by the income-velocity of money and that there is no obvious reason why a reduction in money-wages would reduce either the quantity of money or its income-velocity. Or they may even argue that profits will necessarily go up because wages have gone down. But it would, I think, be more usual to agree that the reduction in money-wages may have *some* effect on aggregate demand through its reducing the purchasing power of some of the workers, but that the real demand of other factors, whose money incomes have not been reduced, will be stimulated by the fall in prices, and that the aggregate demand of the workers themselves will be very likely increased as a result of the increased volume of employment, unless the elasticity of demand for labour in response to changes in money-wages is less than unity. Thus in the new equilibrium there will be more employment than there would have been otherwise except, perhaps, in some unusual limiting case which has no reality in practice.

It is from this type of analysis that I fundamentally differ; or rather from the analysis which seems to lie behind such observations as the above. For whilst the above fairly represents, I think, the way in which many economists talk and write, the underlying analysis has seldom been written down in detail.

It appears, however, that this way of thinking is probably reached as follows. In any given industry we have a demand schedule for the product relating the quantities which can be sold to the prices asked; we have a series of supply schedules relating the prices which will be asked for the sale of different quantities on various bases of cost; and these schedules between them lead up to a further schedule which, on the assumption that other costs are unchanged (except as a result of the change in output), gives us the demand schedule for labour in the industry relating the quantity of employment to different levels of wages, the shape of the curve at any point furnishing the elasticity of demand for labour. This conception is then transferred without substantial modification to industry as a whole; and it is supposed, by a parity of reasoning, that we have a demand schedule for labour in industry as a whole relating the quantity of employment to different levels of wages. It is held that it makes no material difference to this argument whether it is in terms of money-wages or of real wages. If we are thinking in terms of money-wages, we must, of course, correct for changes in the value of money; but this leaves the general tendency of the argument unchanged, since prices certainly do not change in exact proportion to changes in money-wages.

If this is the groundwork of the argument (and, if it is not, I do not know what the groundwork is), surely it is fallacious. For the demand schedules for particular industries can only be constructed on some fixed assumption as to the nature of the demand and supply schedules of other industries and as to the amount of the aggregate effective demand. It is invalid, therefore, to transfer the argument to industry as a whole unless we also transfer our assumption that the aggregate effective demand is fixed. Yet this assumption reduces the argument to an *ignoratio elenchi*. For, whilst no one would wish to deny the proposition that a reduction in money-wages *accompanied by the same ggregate effective demand as before* will be associated with an increase in employment, the precise question at issue is whether the reduction in money-wages will or will not be accompanied by the same aggregate effective demand as before measured in money, or, at any rate, by an aggregate effective demand which is not reduced in full proportion to the reduction in money-wages (*i.e.* which is somewhat greater measured in wage-units). But if the classical theory is not allowed to extend by analogy its conclusions in respect of a particular industry to industry as a whole, it is wholly unable to answer the question what effect on employment a reduction in money-wages will have. For it has no method of analysis wherewith to tackle the problem. Professor Pigou's *Theory of Unemployment* seems to me to get out of the Classical Theory all that can be got out of it; with the result that the book becomes a striking demonstration that this theory has nothing to offer, when it is applied to the problem of what determines the volume of actual employment as a whole.[1]

II

Let us, then, apply our own method of analysis to answering the problem. It falls into two parts. (1) Does a reduction in money-wages have a direct tendency, *cet. par.,* to increase employment, "*cet. par*." being taken to mean that the propensity to consume, the schedule of the marginal efficiency of capital and the rate of interest are the same as before for the community as a whole? And (2) does a reduction in money-wages have a certain or probable tendency to affect employment in a particular direction through its certain or probable repercussions on these three factors?

The first question we have already answered in the negative in the preceding chapters. For we have shown that the volume of employment is uniquely correlated with the volume of effective demand measured in wage-units, and that the effective demand, being the sum of the expected consumption and the expected investment, cannot change, if the propensity to consume, the schedule of marginal efficiency of capital and the rate of interest are all unchanged. If, without any change in these factors, the entrepreneurs were to increase employment as a whole, their proceeds will necessarily fall short of their supply-price.

Perhaps it will help to rebut the crude conclusion that a reduction in money-wages will increase employment "because it reduces the cost of production", if we follow up the course of events on the hypothesis most favourable to this view, namely that at the outset entrepreneurs *expect* the reduction in money-wages to have this effect. It is indeed not unlikely that the individual entrepreneur, seeing his own costs reduced, will overlook at the outset the repercussions on the demand for his product and will act on the assumption that he will be able to sell at a profit a larger output than before. If, then, entrepreneurs generally act on this expectation, will they in fact succeed in increasing their profits? Only if the community's marginal propensity to consume is equal to unity, so that there is no gap between the increment of income and the increment of consumption; or if there is an increase in investment, corresponding to the gap between the increment of income and the increment of consumption, which will only occur if the schedule of marginal efficiencies of capital has increased relatively to the rate of interest. Thus the proceeds realised from the increased output will disappoint the entrepreneurs and employment will fall back again to its previous figure, unless the marginal propensity to consume is equal to unity or the reduction in money-wages has had the effect of increasing the schedule of marginal efficiencies of capital relatively to the rate of interest and hence the amount of investment. For if entrepreneurs offer employment on a scale which, if they could sell their output at the expected price, would provide the public with incomes out of which they would save more than the amount of current investment, entrepreneurs are bound to make a loss equal to the difference; and this will be the case absolutely irrespective of the level of money wages. At the best, the date of their disappointment can only be delayed for the interval during which their own investment in increased working capital is filling the gap.

Thus the reduction in money-wages will have no lasting tendency to increase employment except by virtue of its repercussions either on the propensity to consume for the community as a whole, or on the schedule of marginal efficiencies of capital, or on the rate of interest. There is no method of analysing the effect of a reduction in money-wages, except by following up its possible effects on these three factors.

The most important repercussions on these factors are likely, in practice, to be the following:

(1) A reduction of money-wages will somewhat reduce prices. It will, therefore, involve some redistribution of real income (*a*) from wage-earners to other factors entering into marginal prime cost whose remuneration has not been reduced, and (*b*) from entrepreneurs to rentiers to whom a certain income fixed in terms of money has been guaranteed.

What will be the effect of this redistribution on the propensity to consume for the community as a whole? The transfer from wage-earners to other factors is likely to diminish the propensity to consume. The effect of the transfer from entrepreneurs to rentiers is more open to doubt. But if rentiers represent on the whole the richer section of the community and those whose standard of life is least flexible, then the effect of this also will be unfavourable. What the net result will be on a balance of considerations, we can only guess. Probably it is more likely to be adverse than favourable.

(2) If we are dealing with an unclosed system, and the reduction of money-wages is a *reduction relatively to money-wages abroad* when both are reduced to a common unit, it is evident that the change will be favourable to investment, since it will tend to increase the balance of trade. This assumes, of course, that the advantage is not offset by a change in tariffs, quotas, etc. The greater strength of the traditional belief in the efficacy of a reduction in money-wages as a means of increasing employment in Great Britain, as compared with the United States, is probably attributable to the latter being, comparatively with ourselves, a closed system.

(3) In the case of an unclosed system, a reduction of money-wages, though it increases the favourable balance of trade, is likely to worsen the terms of trade. Thus there will be a reduction in real incomes, except in the case of the newly employed, which may tend to increase the propensity to consume.

(4) If the reduction of money-wages is expected to be a *reduction relatively to money-wages in the future,* the change will be favourable to investment, because as we have seen above, it will increase the marginal efficiency of capital; whilst for the same reason it may be favourable to consumption. If, on the other hand, the reduction leads to the expectation, or even to the serious possibility, of a further wage-reduction in prospect, it will have precisely the opposite effect. For it will diminish the marginal efficiency of capital and will lead to the postponement both of investment and of consumption.

(5) The reduction in the wages-bill, accompanied by some reduction in prices and in money-incomes generally, will diminish the need for cash for income and business purposes; and it will therefore reduce *pro tanto* the schedule of liquidity-preference for the community as a whole. *Cet. par.* this will reduce the rate of interest and thus prove favourable to investment. In this case, however, the effect of expectation concerning the future will be of an opposite tendency to those just considered under (4). For, if wages and prices are expected to rise again later on, the favourable reaction will be much less pronounced in the case of long-term loans than in that of short-term loans. If, moreover, the reduction in wages disturbs political confidence by causing popular discontent, the increase in Liquidity preference due to this cause may more than offset the release of cash from the active circulation.

(6) Since a special reduction of money-wages is always advantageous to an individual entrepreneur or industry, a general reduction (though its actual effects are different) may

also produce an optimistic tone in the minds of entrepreneurs, which may break through a vicious circle of unduly pessimistic estimates of the marginal efficiency of capital and set things moving again on a more normal basis of expectation. On the other hand, if the workers make the same mistake as their employers about the effects of a general reduction, labour troubles may offset this favourable factor; apart from which, since there is, as a rule, no means of securing a simultaneous and equal reduction of money-wages in all industries, it is in the interest of all workers to resist a reduction in their own particular case. In fact, a movement by employers to revise money-wage bargains downward will be much more strongly resisted than a gradual and automatic lowering of real wages as a result of rising prices.

(7) On the other hand, the depressing influence on entrepreneurs of their greater burden of debt may partly offset any cheerful reactions from the reduction of wages. Indeed if the fall of wages and prices goes far, the embarrassment of those entrepreneurs who are heavily indebted may soon reach the point of insolvency, — with severely adverse effects on investment. Moreover the effect of the lower price-level on the real burden of the National Debt and hence on taxation is likely to prove very adverse to business confidence.

This is not a complete catalogue of all the possible reactions of wage reductions in the complex real world. But the above cover, I think, those which are usually the most important.

If, therefore, we restrict our argument to the case of a closed system, and assume that there is nothing to be hoped, but if anything the contrary, from the repercussions of the new distribution of real incomes on the community's propensity to spend, it follows that we must base any hopes of favourable results to employment from a reduction in money-wages mainly on an improvement in investment due either to an increased marginal efficiency of capital under (4) or a decreased rate of interest under (5). Let us consider these two possibilities in further detail.

The contingency, which is favourable to an increase in the marginal efficiency of capital, is that in which money-wages are believed to have touched bottom, so that further changes are expected to be in the upward direction. The most unfavourable contingency is that in which money-wages are slowly sagging downwards and each reduction in wages serves to diminish confidence in the prospective maintenance of wages. When we enter on a period of weakening effective demand, a sudden large reduction of money-wages to a level so low that no one believes in its indefinite continuance would be the event most favourable to a strengthening of effective demand. But this could only be accomplished by administrative decree and is scarcely practical politics under a system of free wage-bargaining. On the other hand, it would be much better that wages should be rigidly fixed and deemed incapable of material changes, than that depressions should be accompanied by a gradual downward tendency of money-wages, a further moderate wage reduction being expected to signalise each increase of, say, 1 per cent. in the amount of unemployment. For example, the effect of an expectation that wages are going to sag by, say, 2 per cent. in the coming year will be roughly equivalent to the effect of a rise of 2 per cent. in the amount of interest payable for the same period. The same observations apply *mutatis mutandis* to the case of a boom.

It follows that with the actual practices and institutions of the contemporary world it is more expedient to aim at a rigid money-wage policy than at a flexible policy responding by easy stages to changes in the amount of unemployment; — so far, that is to say, as the marginal efficiency of capital is concerned. But is this conclusion upset when we turn to the rate of interest?

It is, therefore, on the effect of a falling wage- and price-level on the demand for money that those who believe in the self-adjusting quality of the economic system must rest the weight of their argument; though I am not aware that they have done so. If the quantity of money is itself a function of the wage- and price-level, there is indeed, nothing to hope in this direction. But if the quantity of money is virtually fixed, it is evident that its quantity in terms of wage-units can be indefinitely increased by a sufficient reduction in money-wages; and that its quantity in proportion to incomes generally can be largely increased, the limit to this increase depending on the proportion of wage-cost to marginal prime cost and on the response of other elements of marginal prime cost to the falling wage-unit.

We can, therefore, theoretically at least, produce precisely the same effects on the rate of interest by reducing wages, whilst leaving the quantity of money unchanged, that we can produce by increasing the quantity of money whilst leaving the level of wages unchanged. It follows that wage reductions, as a method of securing full employment, are also subject to the same limitations as the method of increasing the quantity of money. The same reasons as those mentioned above, which limit the efficacy of increases in the quantity of money as a means of increasing investment to the optimum figure, apply *mutatis mutandis* to wage reductions. Just as a moderate increase in the quantity of money may exert an inadequate influence over the long-term rate of interest, whilst an immoderate increase may offset its other advantages by its disturbing effect on confidence; so a moderate reduction in money-wages may prove inadequate, whilst an immoderate reduction might shatter confidence even if it were practicable.

There is, therefore, no ground for the belief that a flexible wage policy is capable of maintaining a state of continuous full employment; — any more than for the belief than an open-market monetary policy is capable, unaided, of achieving this result. The economic system cannot be made self-adjusting along these lines.

If, indeed, labour were always in a position to take action (and were to do so), whenever there was less than full employment, to reduce its money demands by concerted action to whatever point was required to make money so abundant relatively to the wage-unit that the rate of interest would fall to a level compatible with full employment, we should, in effect, have monetary management by the Trade Unions, aimed at full employment, instead of by the banking system.

Nevertheless while a flexible wage policy and a flexible money policy come, analytically, to the same thing, inasmuch as they are alternative means of changing the quantity of money in terms of wage-units, in other respects there is, of course, a world of difference between them. Let me briefly recall to the reader's mind the three outstanding considerations.

(i) Except in a socialised community where wage-policy is settled by decree, there is no means of securing uniform wage reductions for every class of labour. The result can only be brought about by a series of gradual, irregular changes, justifiable on no criterion of social justice or economic expediency, and probably completed only after wasteful and disastrous struggles, where those in the weakest bargaining position will suffer relatively to the rest. A change in the quantity of money, on the other hand, is already within the power of most governments by open-market policy or analogous measures. Having regard to human nature and our institutions, it can only be a foolish person who would prefer a flexible wage policy to a flexible money policy, unless he can point to advantages from the former which are not obtainable from the latter. Moreover, other things being equal, a method which it is comparatively easy to apply should be deemed preferable to a method which is probably so difficult as to be impracticable.

(ii) If money-wages are inflexible, such changes in prices as occur (*i.e.* apart from "administered " or monopoly prices which are determined by other considerations besides marginal cost) will mainly correspond to the diminishing marginal productivity of the existing equipment as the output from it is increased. Thus the greatest practicable fairness will be maintained between labour and the factors whose remuneration is contractually fixed in terms of money, in particular the rentier class and persons with fixed salaries on the permanent establishment of a firm, an institution or the State. If important classes are to have their remuneration fixed in terms of money in any case, social justice and social expediency are best served if the remunerations of *all* factors are somewhat inflexible in terms of money. Having regard to the large groups of incomes which are comparatively inflexible in terms of money, it can only be an unjust person who would prefer a flexible wage policy to a flexible money policy, unless he can point to advantages from the former which are not obtainable from the latter.

(iii) The method of increasing the quantity of money in terms of wage-units by decreasing the wage-unit increases proportionately the burden of debt; whereas the method of producing the same result by increasing the quantity of money whilst leaving the wage unit unchanged has the opposite effect. Having regard to the excessive burden of many types of debt, it can only be an inexperienced person who would prefer the former.

(iv) If a sagging rate of interest has to be brought about by a sagging wage-level, there is, for the reasons given above, a double drag on the marginal efficiency of capital and a double reason for putting off investment and thus postponing recovery.

III

It follows, therefore, that if labour were to respond to conditions of gradually diminishing employment by offering its services at a gradually diminishing money-wage, this would not, as a rule, have the effect of reducing real wages and might even have the effect of increasing them, through its adverse influence on the volume of output. The chief result of this policy would be to cause a great instability of prices, so violent perhaps as to make business calculations futile in an economic society functioning after the manner of that in which we live. To suppose that a flexible wage policy is a right and proper adjunct of a system which on the whole is one of *laissez-faire,* is the opposite of the truth. It is only in a highly authoritarian society, where sudden, substantial, all-round changes could be decreed that a flexible wage-policy could function with success. One can imagine it in operation in Italy, Germany or Russia, but not in France, the United States or Great Britain.

If, as in Australia, an attempt were made to fix real wages by legislation., then there would be a certain level of employment corresponding to that level of real wages; and the actual level of employment would, in a closed system, oscillate violently between that level and no employment at all, according as the rate of investment was or was not below the rate compatible with that level; whilst prices would be in unstable equilibrium when investment was at the critical level, racing to zero whenever investment was below it, and to infinity whenever it was above it. The element of stability would have to be found, if at all, in the factors controlling the quantity of money being so determined that there always existed some level of money-wages at which the quantity of money would be such as to establish a relation between the rate of interest and the marginal efficiency of capital which would maintain investment at the critical level. In this event employment would be constant (at the level appropriate to the legal real wage) with money-wages and prices fluctuating rapidly in the degree just necessary to maintain this rate of investment at the appropriate figure. In the actual case of Australia, the escape was found, partly of course in the inevitable inefficacy of the legislation to achieve its object, and partly in Australia not being a closed system, so that the level of money-wages was itself a determinant of the level of foreign investment and hence of total investment, whilst the terms of trade were an important influence on real wages.

In the light of these considerations I am now of the opinion that the maintenance of a stable general level of money-wages is, on a balance of considerations, the most advisable policy for a closed system; whilst the same conclusion will hold good for an open system, provided that equilibrium with the rest of the world can be secured by means of fluctuating exchanges. There are advantages in some degree of flexibility in the wages of particular industries so as to expedite transfers from those which are relatively declining to those which are relatively expanding. But the money-wage level as a whole should be maintained as stable as possible, at any rate in the short period.

This policy will result in a fair degree of stability in the price-level;-greater stability, at least, than with a flexible wage policy. Apart from “administered” or monopoly prices, the price-level will only change in the short period in response to the extent that changes in the volume of employment affect marginal prime costs; whilst in the long period they will only change in response to changes in the cost of production due to new technique and new or increased equipment.

It is true that, if there are, nevertheless, large fluctuations in employment, substantial fluctuations in the price-level will accompany them. But the fluctuations will be less, as I have said above, than with a flexible wage policy.

Thus with a rigid wage policy the stability of prices will be bound up in the short period with the avoidance of fluctuations in employment. In the long period, on the other hand, we are still left with the choice between a policy of allowing prices to fall slowly with the progress of technique and equipment whilst keeping wages stable, or of allowing wages to rise slowly whilst keeping prices stable. On the whole my preference is for the latter alternative, on account of the fact that it is easier with an expectation of higher wages in future to keep the actual level of employment within a given range of full employment than with an expectation of lower wages in future, and on account also of the social advantages of gradually diminishing the burden of debt, the greater ease of adjustment from decaying to growing industries, and the psychological encouragement likely to be felt from a moderate tendency for money-wages to increase. But no essential point of principle is involved, an it would lead me beyond the scope of my present purpose to develop in detail the arguments on either side.

Author's Footnotes

1. In an appendix to this chapter Professor Pigou's *Theory of Unemployment* is criticised in detail.

Contents | Appendix on Unemployment | Keynes Archive

10/28

Keynes Reaction

Michael Plasmeier

John Maynard Keynes' views have taken over the world. Economics 101 is basically his theories. To be fair, his theories seem to be more nuanced than the classical economists who came before. For example, instead of just making a sweeping assumption that wages are fluid, Keynes looks a bit more into the details and says that wages are actually not fluid, but people resist them lowering. We can see a perfect example in the protests ongoing in Greece. Furthermore, there is a distinction between real and nominal wages.

Plus Keynes adds the possibility that people might choose to save – not just consume immediately. Plus consumers are even more likely to do so if they think the economy will get worse in the future. Plus, businesses do not want to invest, even though interest rates are lower because they don't think they need to grow capacity.

The whole study of what causes what to move is fascinating. The graphs which came out of the IS-LM models helps us understand these concepts better than just the written word, since it allows to visualize the changes better.

Michael E Plasmeier

From: Vincent Pons <vpons@MIT.EDU>
Sent: Sunday, October 28, 2012 2:18 PM
To: Vincent Pons
Subject: [14.72] 14.72 - topics of the next classes and 2nd essay

Follow Up Flag: Follow up
Flag Status: Flagged

Dear all,

Michael has asked me to send the following note:
* contrary to what was said in last class, Keynes (and not Polanyi) will be discussed on Monday. Michael will cover Keynes largely in a lecture format on Monday. We will discuss Polanyi on Wednesday and you should concentrate on reading that. If you don't get to the Keynes before Monday's class, you can pick it up afterwards.
* The second paper topic has been posted on Stellar. The due date has been moved foward, to November 9th.

best,
Vincent

14.72 10/31

Last class cancled w/ Hurricane

He will rearrange readings

Today: Keynes

Mon: Polani

Afterwards: See restructured sechedule - TBD

Don't read ahead

Keynes

Paradigm in itself

Paradigm in econ.

L self concious break from old paradigm

Show how Keynes is a paradigm

Picture of his global vision of econ

2

Why now: Explaining humans as embeded in social env
Understand econ by how ind make decision
Ind interact w/ each other directly in a social env

Understand in terms of <u>great depression</u>
like 2008 recession
began w/ fin crisis → 1929
ed in real econ
deep depression - diff than anything before
econ sank 1941-1943
hit bottom & stayed there

trap
keynes had an explination for each stage
We mostly think about Stage 3 → staying at bottom
keyenes wrote a lot abat Stage 1: fin crisis

~~4~~ 3.

"Rediscovered" in 08 the financial writing

Very high levels of unemp + all resources underused

Lots of theories

gehto alinated from society

Youth unexperienced

but here it was the core of the great depression

normal economics is all about unlim ~~ear~~ demand

and limited resources

but all these resources just sitting around!

how do you explain that?

World of limited resources

Say's Law: supplies creates own demand

so can't have unused resources

national income accounting

$GDP = \sum P_i Q_i = PQ = \underbrace{Wages}_{\text{pay out}} + Rent + Interest + \ldots + \Pi$

(4)

π is the residual

Says' Law is that

But must spend what they get paid

Bound to spend the \$

Say: Money is just a convience

to facilitate transactions

not worth anything itself

People interested in real goods

Marx: $C \to M \to C'$

vs

$M \to C \to M'$

like the fetishm of commodity

not focused on use value

Marx: natural to get stuck in \$

(5)

but could produce wrong type of goods
too much butter + not enough guns

will be price adjustments

Keynes: those mechanisms don't work
Say's Law does not matter

Savings vs Investment

If save + people invest → completes Say's law anyway

Interest is price of $

Price that person providing savings gets paid

Same for Say's Law on Savings + Investment

$S = I$

↑ like any other goods

So still same mechanism

6

Keynes focused on 2 markets
where prices would not bring things into balance

- Savings + investment

Me: People uncertain of future

Prof: Interest rate can't fall any further than 0

What is the price of savings?

Not i, but fear about the future

i close to 0 - but fearful of future

- Labor market wage rates not that responsive

expect unemployed resources => prices fall

People hire more + more labor

People rather be unemployed than lower wages

~~Me~~ Me: People don't want that

Prof: You are making up reasons

* It's since people sitting in social/political world

7

Keynes: People care more about relative wage
↳ relative to other people

deflationary period → can't cut wages
People resist cuts to their social condition.

Keynes: income on future based on expectations
↳ comes through interactions w/ others
*

He put in place whole new political apparatus

GDP $\sum P_i Q = PQ$ = Wages + interest + rent + ... trust

↑ think in terms of industry

↑ think in terms of income

Keynes: lets do GDP a diff way w/ new categories
GDP = C + I + G ← his main contribution

(8)

So why nobel prize for this?

each involved diff theories

C, I, G — theory of consumption

— " " investment

— " " gov

Full employment GDP vs actual GDP

$GDP_{FE} - GDP(\ ) = GAP$

Keynes: Had to change C, I, so change G

We know know other things you can do:

— tax cuts fall under C → not really G

: G is spending − taxes

So kinda

w/ debt → Complicated

— (missed)

* so instead of adjusting prices

↳ adjust quantity

Sep set of behavioral understandings for each

That is Keynesian econ ~~ea~~ as a paradigm

Conventional: uniform system CF, G
prices
market

After war: price system not working
We will look at macro this way
but look at ~~...~~ markets for micro

So hybrid economics system

↓

neoclassical synthesis

macro: keynsian
micro: normal market

(10)

Classical
neoclassical
keynsian

$\xrightarrow{\text{micro}}$ $\nearrow_{\text{macro}}$ = neoclassical synthesis

↑ the "synthesis" distiction is key

But this is not kuhn-like for paradigm
Prof i makes economics skitophrenic

Most important thing in econ; explain great depression
So no one cared too much about contridiction

Until his generation started thinking about it

Was central thrust of econ research ~1975

Can reconstruct ~~macro alone~~ macro or micro so like other
try to reconstruct macro so consistent w/ neoclassical
(i.e. or did he say micro?)

Most clear example; Phillips Curve

11

Unemployment vs inflation

(missed)

End of war vindicated Keynes

G↑ enough to get us out of depression

balance b/w inflation + unemployment w/ right level of gov expenditures

What do you choose → unemp or inflation?

Freedman + Lucas say Phillips curve

← only 1 level consistent w/ price stability

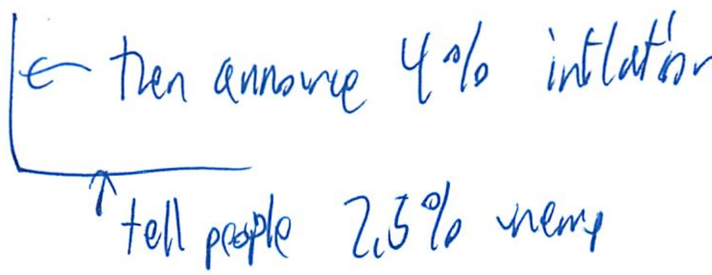
↑ the non inflationary (NRU) level

rational expectations

(12)

Phillips observed his curve
happened by accident

But Friedman: If trying to do by policy



Announcing inflation → people will anticipate
this moves up the phillips curve

I don't know where draw dotted so like 

So ask for 8% if think 4% inflation

~~So Unemp~~ is
not that unemp is fixed
but if try to do this, inflation will accelerate

(13)

So what does that mean for Keynes' theory?

- can't treat G as seperate
  - Keynes' Phillips Curve made it look like people were not rational actors

Friedman: Private sector will react + compensate for gov actions.

(need to look at more → not fully getting it)

Friedman: G is not sep from I, C
↳ rational behavior of market

made macro more like neoclassical (which was used for micro)
pointed in that direction → didn't actually solve problem

Karl Polanyi

10/29

From Wikipedia, the free encyclopedia

Karl Paul Polanyi (Hungarian: *Polányi Károly* [ˈpolaːɲi ˈkaːroj]; born October 25, 1886, Vienna, Austro-Hungarian Empire – April 23, 1964, Pickering, Ontario)[1] was a Hungarian economic historian, economic anthropologist and social philosopher known for his opposition to traditional economic thought and his book, *The Great Transformation*. Polanyi is remembered today as the originator of substantivism, a cultural approach to economics, which emphasized the way economies are embedded in society and culture. This view ran counter to mainstream economics but was popular in anthropology, economic history, economic sociology and political science.

Polanyi's approach to the ancient economies has been applied to a variety of cases, such as Pre-Columbian America and ancient Mesopotamia, although its utility to the study of ancient societies in general has been questioned.[2] Polanyi's *The Great Transformation* became a model for historical sociology. His theories eventually became the foundation for the economic democracy movement. His daughter Kari Polanyi-Levitt is Emerita Professor of Economics at McGill University, Montreal.

Contents

Life

Early life

See also: Polányi

Polanyi was born into a Jewish family. His younger brother was chemist and philosopher Michael Polanyi, and was born in Vienna, at the time the capital of the Austro-Hungarian Empire. Mihály Pollacsek father of Karl and Michael Polanyi, was a railway entrepreneur. He never changed the name Pollacsek and is buried in the Jewish cemetery in Budapest. Karl and Michael Polanyi's mother was Cecília Wohl. The name change to Polanyi (not von Polanyi) was effected by Karl and his siblings. Polanyi was well educated despite the ups and downs of his father's fortune, and he immersed himself in Budapest's active intellectual and artistic scene.

Polanyi founded the radical and influential Club Galilei while at the University of Budapest, a club which would have far reaching effects on Hungarian intellectual thought. During this time, he was actively engaged with other notable thinkers, such as György Lukács, Oszkár Jászi, and Karl Mannheim. Polanyi graduated from Budapest University in 1912 with a doctorate in Law. In 1914 he helped found the Hungarian Radical Party and served as its secretary.

Polanyi was a cavalry officer the Austro-Hungarian Army in World War I, in active service at the Russian Front and hospitalized in Budapest. Polanyi supported the Republican government of Mihály Károlyi and its Social Democratic regime. The republic was short-lived, however, and when Béla Kun toppled the Karolyi government to create the Hungarian Soviet Republic Polanyi left for Vienna.

From 1924 to 1933 he was employed as a senior editor of the prestigious *Der Oesterreichische Volkswirt* ('The Austrian Economist'). It was at this time that he first began criticizing the Austrian School of economists, who he felt created abstract models which lost sight of the organic, interrelated reality of economic processes. Polanyi himself was attracted to Fabianism and the works of G. D. H. Cole. It was also during this period that Polanyi grew interested in Christian Socialism.

He married the communist revolutionary Ilona Duczynska, of Polish-Hungarian background.

United States and Canada

Polanyi was asked to resign from the Oesterreichische Volkswirt because the liberal publisher of the Journal could not keep a prominent socialist, after the accession of Hitler to office in January 1933 and the suspension of the Austrian parliament by the rising tide of clerical fascism in Austria. He left for London in 1933 where he earned a living as a journalist and tutor and obtained a position as a lecturer for the Workers' Educational Association in 1936. His lecture notes contained the research for what later became *The Great Transformation*. However, he would not start writing this work until 1940, when he moved to Vermont to take up a position at Bennington College. The book was published in 1944 to great acclaim. In it, Polanyi described the enclosure process in England and the creation of the contemporary economic system at the beginning of the 19th century.

After the war Polanyi received a teaching position at Columbia University (1947-1953). However, his wife's (Ilona Duczynska) background as a former communist made gaining an entrance visa in the United States impossible. As a result they moved to Canada, and Polanyi commuted to New York City. In the early 1950s Polanyi received a large grant from the Ford Foundation to study the economic systems of ancient empires.

Having described the emergence of the modern economic system, Polanyi now sought to understand how "the economy" emerged as a distinct sphere in the distant past. His seminar at Columbia drew several famous scholars and influenced a generation of teachers, resulting in the 1957 volume *Trade and Markets in the Early Empires*. Polanyi continued to write in his later years and established a new journal entitled *Coexistence*. In Canada he resided in Pickering, Ontario, where he died in 1964.

Works

- *The Great Transformation* (1944)
- *Trade and Markets in the Early Empires* (1957, edited and with contributions by others)
- *Dahomey and the Slave Trade* (1966)
- *Primitive, Archaic, and Modern Economics: Essays of Karl Polanyi* (1968, collected essays and selections from his work).
- *The Livelihood of Man (Studies in social discontinuity)(Academic Pr; New Ed edition (November 1977)*

The Great Transformation (book)

From Wikipedia, the free encyclopedia

10/29

The Great Transformation is a book by Karl Polanyi, an Austro-Hungarian political economist. First published in 1944, it deals with the social and political upheavals that took place in England during the rise of the market economy. Polanyi contends that the modern market economy and the modern nation-state should be understood not as discrete elements, but as the single human invention he calls the "Market Society".

economy + state together

↳ Do we take this for granted

Contents

General argument

Polanyi argued that the development of the modern state went hand in hand with the development of modern market economies and that these two changes were inexorably linked in history. His reasoning for this was that the powerful modern state was needed to push changes in social structure that allowed for a competitive capitalist economy, and that a capitalist economy required a strong state to mitigate its harsher effects. For Polanyi, these changes implied the destruction of the basic social order that had existed throughout all earlier history, which is why he emphasized the greatness of the transformation. *

landed gentry ? see pg

His empirical case in large part relied upon analysis of the Speenhamland laws, which he saw not only as the last attempt of the squirearchy to preserve the traditional system of production and social order, but also a self-defensive measure on the part of society that mitigated the disruption of the most violent period of economic change. The book also presented his belief that market society is unsustainable because it is fatally destructive to the human and natural contexts it inhabits.

ie their self interest - save their skins

Polanyi turns the tables on the orthodox liberal account of the rise of capitalism by arguing that "laissez-faire was planned", whereas social protectionism was a spontaneous reaction to the social dislocation imposed by an unrestrained free market. He argues that the construction of a 'self-regulating' market necessitates the separation of society into economic and political realms. Polanyi does not deny that the self-regulating market has brought "unheard of material wealth", however he suggests that this is too narrow a focus. The market, once it considers land, labor and money as "fictitious commodities" (fictitious because each possesses qualities that are not expressed in the formal rationality of the market) "subordinate[s] the substance of society itself to the laws of the market."[1]

What were the diff realms?

This, he argues, results in massive social dislocation, and spontaneous moves by society to protect itself. In effect, Polanyi argues that once the free market attempts to separate itself from the fabric of society, social protectionism is society's natural response; this he calls the 'double movement'. Polanyi did not see economics as a subject closed off from other fields of enquiry, indeed he saw economic and social problems as inherently linked. He ended his work with a prediction of a socialist society, noting, "after a century of blind 'improvement', man is restoring his 'habitation.'"[2]

Before Market Society

Polanyi makes the distinction between markets as an auxiliary tool for ease of exchange of goods and Market Societies. Market Societies are those where markets are the paramount institution for the exchange of goods through price mechanisms. Polanyi argues that there are three general types of economic systems that existed before the rise of a society based on a free market economy: Redistributive, Reciprocity and Householding.

1. Redistributive: Trade and production is focused to a central entity such as a tribal leader or feudal lord and then redistributed to members of their society.
2. Reciprocity: The exchange of goods is based on reciprocal exchanges between social entities. On a macro level this would include the production of goods to gift to other groups.
3. Householding: Economies where production is centered around individual household production. Family units produce food, textile goods, and tools for their own consumption.

These three forms were not mutually exclusive nor were they mutually exclusive of markets for the exchange of goods. The main distinction is that these three forms of economic organization were based around the social aspects of the society they operated in and were explicitly tied to those social relationships. Polanyi argued that these economic forms depended on the social principles of Centricity and Symmetry and Autarky (Self-Sufficiency). Markets existed as an auxiliary avenue for the exchange of goods that were otherwise not obtainable. They relied on the social Principles of Centricity and Symmetry.

Publication details

The book was originally published in the United States in 1944 and then in England in 1945 as *The Origins of Our Time*. It was reissued by Beacon Press as a paperback in 1957 and as a 2nd edition with a foreword by Joseph Stiglitz in 2001.[3]

Polanyi, K. (1944). The great transformation. New York: Rinehart.[4]

Polanyi, K. (1957). The great transformation. Boston: Beacon Press.[5]

Polanyi, K. (2001). The great transformation: The political and economic origins of our time. Boston: Beacon Press.[6]

Reviews

Clough, S. B., & Polanyi, K. (1944). Review of The Great Transformation. *The Journal of Modern History*, 16, December, 4, 313-314.[*citation needed*]

Block, F., & Polanyi, K. (2003). Karl Polanyi and the Writing of "The Great Transformation". Theory and

Substantivism

From Wikipedia, the free encyclopedia

Substantivism is a position, first proposed by Karl Polanyi in his work *The Great Transformation*, which argues that the term 'economics' has two meanings. The formal meaning, used by today's neoclassical economists, refers to economics as the logic of rational action and decision-making, as rational choice between the alternative uses of limited (scarce) means, as 'economising,' 'maximizing,' or 'optimizing.' [1]

The second, substantive meaning presupposes neither rational decision-making nor conditions of scarcity. It refers to how humans make a living interacting within their social and natural environments. A society's livelihood strategy is seen as an adaptation to its environment and material conditions, a process which may or may not involve utility maximisation. The substantive meaning of 'economics' is seen in the broader sense of 'provisioning.' Economics is the way society meets material needs.[1]

References

1. ^ a b Polanyi, Karl. (1944) *The Great Transformation: the Political and Economic Origins of Our Time*, Farrar and Rinehart, New York

So what? That economics could mean something else beside optimizing

See also

- Economic anthropology

Retrieved from "http://en.wikipedia.org/w/index.php?title=Substantivism&oldid=500910697"
Categories: Economics terminology | Economic anthropology | Anthropology stubs

- This page was last modified on 6 July 2012 at 06:44.
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Speenhamland system

From Wikipedia, the free encyclopedia
(Redirected from Speenhamland)

10/29

The **Speenhamland system** was a form of outdoor relief intended to mitigate rural poverty in England at the end of the 18th century and during the early 19th century. The law was an amendment to the Elizabethan Poor Law. It was created as an indirect result of Britain's involvements in the French Revolutionary and Napoleonic Wars (1793–1815).[*citation needed*] The system was named after a 1795 meeting at the Pelican Inn in Speenhamland, Berkshire, where a number of local magistrates devised the system as a means to alleviate the distress caused by high grain prices. The increase in the price of grain most probably occurred as a result of a poor harvest in the years 1795–96, though at the time this was subject to great debate. Many blamed middlemen and hoarders as the ultimate architects of the shortage.

welfare

The authorities at Speenhamland approved a means-tested sliding-scale of wage supplements in order to mitigate the worst effects of rural poverty. Essentially, families were paid extra to top up wages to a set level according to a table. This level varied according to the number of children and the price of bread. For example, if bread was 1s 2d a loaf, the wages of a family with two children were topped up to 8s 6d. If bread rose to 1s 8d the wages were topped up to 11s 0d.

Speenhamland has been seen to aggravate the underlying causes of poverty in any particular parish, but more recent research has shown that it helped prevent chronic poverty and malnutrition, thus avoiding declining productivity in the workforce. The immediate impact of paying the poor rate fell on the landowners of the parish concerned. They then sought other means of dealing with the poor, such as the workhouse funded through parish unions. Eventually pressure due to structural poverty caused the introduction of the new Poor Law (1834).

The Speenhamland system appears to have reached its height during the Napoleonic Wars, when it was a means of allaying dangerous discontent amongst a growing rural proletariat faced by soaring food prices, and to have died out in the post-war period, except in a few parishes.[1] The system was popular in the south of England. William Pitt the Younger attempted to get the idea passed into legislation but failed. The system was not adopted nationally but was popular in the counties which experienced the Swing Riots during the 1830s.

Contents

Criticisms

The Poor Law Commissioners' Report of 1834 called the Speenhamland System a "universal system of pauperism". The system allowed employers (often farmers) to pay below subsistence wages, because the parish would make up the difference and keep their workers alive. So the workers' low income was unchanged and the poor rate contributors subsidised the farmers. General welfare arguments

Thomas Malthus believed a system of supporting the poor would lead to increased population growth rates because the Poor Laws encouraged early marriage. No empirical evidence shows a strong correlation between population rates and Speenhamland though.

This system of poor relief, and others like it, lasted until the passing of the Poor Law Amendment Act 1834.

Evidence in the last thirty years shows that the bread scale devised during the Speenhamland meeting in 1795 was by no means universal, and that even the system of outdoor relief which found one of its earliest, though not the first, expressions in Speenhamland was not completely widespread. Allowances, or supplements, to wages were used generally as a temporary measure, and the nature of their execution changed in various regions. Mark Blaug's classic 1960 essay *The Myth of the Old Poor Law* charged the commissioners of 1834 with largely using the Speenhamland system to vilify the old poor law and create will for the passage of a new one.

Historical interpretations

Speenhamland appears to have been one among many systems of bread scales, but it most likely owes its notoriety to Frederick Eden's *The State of the Poor* (1797). Eden attacked the system as an impediment to agricultural progress. Though some of Blaug's more drastic assertions may be ill-founded or overly polemical, it appears evident that Speenhamland was by no means a household name, and that since the practice was by January 1795 (the famous meeting was in May) being used in various villages, usually in collusion with other means of relieving the poor. Because of failed attempts to reform the existing poor law at a national level, the scarcity of 1795 was largely dealt with by innovations in a haphazard way at the local level, and it seems improbable that a national and uniform policy existed.

See also

- Earned income tax credit
- Roundsman
- Labour Rate
- Poor Law
- Timeline of children's rights in the United Kingdom
- NREGA

References

1. ^ Phillis Deane (1965) *The First Industrial Revolution* Cambridge: Cambridge Press. p144. ISBN 0-521-29609-9

Further reading

- Poynter, J. R. *Society and Pauperism*
- Thompson, E. P. *The Making of the English Working Class*

The Great Transformation

Karl Polanyi

Foreword by Robert M. MacIver

Beacon Press Boston

Read 10/29

1944

10/29

Polanyi Reaction

Michael Plasmeier

Karl Polanyi argues that the economy and the state are linked. For example, each class tries to gain political power in order to help each's own interest. The rich does this with money, while the poor do this with votes.

I think part of the move from individualistic to collectivistic – for example, the reason behind workman's compensation - is that as a society we trade off pure profits for stability and cultural adhesion. As an individual, we smooth out the peaks and valleys in our wealth by buying insurance. Likewise, as a society, we would prefer to smooth out the bumps in the business cycle by implementing counter-cyclic spending measures such as welfare. As such, we shave off the peaks with taxes, and fill the valleys with welfare.

I think the issue of disparities in wealth is also important. We can see that in developed countries, there is less of gap between the rich and poor. Why is that? Is the low income disparity the cause of why wealthy countries' economies are successful (ie. the middle class is buying goods)? Or are they related? Or related the other way? As countries develop do citizens demand more of a say? Or for a society to develop further, it needs more of a middle class? We can see this in India as they achieved rapid economic growth. However the growth has been uneven – not only between the urban and the rural – but through very wealthy barons. Some of this has been because these barons own or run companies who are sheltered from competition through monopolies. Will citizens ever rise up against these monopolies? Is it just a matter of time?

14.72 11/05

(5 min late)

Today: Polani

Shumpter - so don't read

Galbraith + Solow

Wed: ~~Galberg + Social~~ readings + summarize

Next Mon: Off

Next Wed: Piore + Sable

Paper ~~Postpone~~: Fri

Hard Copy Wed

Won't be that hard for extension if you write him

Next Paper Out: Week from Wed

---

3 diff paradigms

1. Liberal/neoclassical
2. Marxist
3. Socological/Antropological

①

a) structure of econ ; set of ideas

Weaber has one set

Paleni diff set

Schumpeter ; diff set

think of humans as embedded in a social structure

no emphasis on individuals

Marx ; start w/ market

econ evolving

in marx but not as much in these

Piore ; Larger + larger enteprises
book Coordinated - like planning

instead of market

Diff explaination of whats going on

But similar evolution of whats going on

(13)

Then this ^{x} what: contridicted by where econ is actually going

Why is econ no longer moving in directions authors say

What actual structures are going on:

Polanyi | Most difficult book

:Most boring:

evolution of capitalism over time

English is not his native lang

Does Polanyi belive in market?

No - but at certain periods it has been

Friedman: market is inherent in people

- but requires a little help from gov

[illegible]

Becker: more pure theory - inherent

(4)

Marx: Market from evolution of technology

~~Polanyi~~

Weber: Protestant Ethics from Protestant

set of ideas from Calvinism

Polanyi set of people who espoused ideas

Were like Friedman

People constructed institutions which

embodied these ideals

---

liberalism is an ideology

described as a science

Creates the institutions that create capitalism

Then what is natural?

humans naturally live in a social setting

3 principles: reciprocity   homesteading

redistribution

(5)

Grow out of relations people have in a community
Those sure communites redistibute income
so no one starves

homesteding : some set of mechanisms to coordinate
production

---

outside of communites humans lose their sense
of community

~~librealism created~~

markets before librealism : goods + commodies
farmers market

librealism created market in : land, labor, money
Those inconsistent w/ establishment & maintenance
of community

Idea of liberalism spread → curtailed community + created
markets in land, labor, and money

6

Still have similar reforms tody

key to market in labor: abolition of
    Speenhamland system

Welfare system
Goal: no one could starve
local parish would support you if you can't
    make a living

    either gave you $ or subsidized your wage
    had to be from that providence/location

~~Repeal~~
abolished 1840
    was ~~[illegible]~~ harming economy
        tied to providence
instead Poor Laws
    distinguished can work from can't work
    had to be in poor house

7

Market for land & ecology
destroy environment
But Polyani thought of env as more of a location for society

Gold Standard
England

England creates market
Destroys society
Remove roots - people moving around
People starve now - community did let that happen before

Society reacts!
Movement towards limiting extent of market
workers — limit on sale of land
political movements — factory labor laws

8

Polanyi : The double movement

Unlike Marx who sees this class warfare
Polanyi : All classes in society begin to react againts
~~B~~ Pesants and Enlighted Industralists
Destroying something central to society

So push to market
and then market is constrained

- WWI end
  Society very disrupted
  lots of unrest
  → go back towards market in 1920s

(9)

Great Depression: Catastrophy of excessive reliance on market

New Deal: restricts market

but less than Communism + Facism

Written in 1944

Market given too much free reign in 20s

So now war has come to an end

Social Security + Welfare System

Aid to Families w/ Dependent Children

widows + orphans

like the Poor Law reform

but then unemployment insurance

people pay into a fund

Can run out

Congress usually extends

but then you become homeless

Pre-Clinton it went ∞

1930s started

Gradual ~~[illegible]~~ creep

Gilder: De facto increase

keeping boyfriends on the side

gradually expanded

Clinton limited it

Only a period for their life

Whole series of protections for people

Keynes/1944 – had found a way to reconcile market + human needs for stability

Tradeoff b/w market + human needs was over?

If read Polanyi in 1950 ↑ could think double movement came to an end

(11)

But then trade unions + welfare more powerful

1960s + 1970s ; explosion of discontent

explosion of many programs

~~Civil~~ civil rights → black workers

Conflict b/w Market + Society

↑ Society exploded a great deal

Students protested – occupied building

Police expelled students

On MIT campus as well

└ making Vietnam weapons

a few MIT students too

60s + 70s ; social pressures – restriction on markets

Usually explained – civil rights movement

– 1865 ~~women's rights~~ Slavery abolished – 1964

White supremacy in South

12

- Party by law + linching
- North not as much
- 1930s : compromise Northern liberals + Southern Conservatives

Social legislation passed, but exempted industries in which blacks worked

- black community mobilized to protest this
- War in Vietnam
- Workers started to protest labor conditions in shops
- women's movement + gay rights can be traced from this

So expansion in social programs

Period of stagflation

70s economy stagnated

(13)

Ronald Reagan: Progressive reasserting of liberalism + market forces

Today: trade unions down to 8% of labor force

Today: Protects individuals from discrimination
but not change nature of socio economic system

---

* Pendulum swings back + forth over time
reaction at either end of pendulum
Last few decades: a more market economy

Obamas' 2008 election ~~[illegible]~~ - For people reading Polanyi - did pendulum swing back towards social protectionism?

---

2 pieces missing

Gold Std
Owenism

Income dist has been expanding since recently
Since 80s gains to top 1%

(24)

Payment for top execs 50x → 250x - 300x
avg worker
So large redistribution
Country ripe ~~for~~ for reaction in other direction
└ Obama 2008:

He limited pay of execs w/ bailout
Joey: timing of policy bad - just incentived to repay loans
Prof: Should have natolized bank
So can't pay it back

Prof: Or was root of problem people at top
of income dist - have to invest somewhere
So invest it in these toxic assets
But all salaries at top of distribution
like Doctors
— Doctors want to go to top position
Will Obama care put gov in control of
entire medical salary structure?

(15)

Doctors can't move out

So how will you manage the econ

Prof: But Obama didn't really move back in 08

Prof: Or maybe they did!

Next time: Gold std

~~[illegible]~~ Owenism

Shumpter - diff than Marxism

? linear movement

? Cyclical movement

BOOKS BY
JOHN KENNETH GALBRAITH

American Capitalism:
The Concept of Countervailing Power
A Theory of Price Control
Economics and the Art of Controversy
The Great Crash, 1929
The Affluent Society
The Liberal Hour
Economic Development
The Scotch
The New Industrial State
The Triumph
Indian Painting
(with Mohinder Singh Randhawa)
Ambassador's Journal
Economics, Peace and Laughter
A China Passage
Economics and the Public Purpose
Money: Whence It Came, Where It Went
The Age of Uncertainty
Almost Everyone's Guide to Economics
The Nature of Mass Poverty
Annals of an Abiding Liberal
A Life in Our Times
The Voice of the Poor
The Anatomy of Power

Read 11/7
took notes
elsewhere

John Kenneth Galbraith

THE NEW INDUSTRIAL STATE

FOURTH EDITION

2AA

Houghton Mifflin Company / Boston
1985

DISCUSSION

Read 11/7
took notes elsewhere

The New Industrial State

or

Son of Affluence

ROBERT M. SOLOW

MORE than once in the course of his new book Professor Galbraith takes the trouble to explain to the reader why its message will not be enthusiastically received by other economists. Sloth, stupidity, and vested interest in ancient ideas all play a part, perhaps also a wish – natural even in tourist-class passengers – not to rock the boat. Professor Galbraith is too modest to mention yet another reason, a sort of jealousy, but I think it is a real factor. Galbraith is, after all, something special. His books are not only widely read, but actually enjoyed. He is a public figure of some significance; he shares with William McChesney Martin the power to shake stock prices by simply uttering nonsense. He is known and attended to all over the world. He mingles with the Beautiful People; for all I know, he may actually be a Beautiful Person himself. It is no wonder that the pedestrian economist feels for him an uneasy mixture of envy and disdain.

There is also an outside possibility that the profession will ignore *The New Industrial State* (Houghton, Mifflin) because it finds the ideas more or less unhelpful. The world can be divided into big-thinkers and little-thinkers. The difference is illustrated by the old story of the couple who had achieved an agreeable division of labor. She made the unimportant decisions: what job he should take, where they should live, how to bring up the children. He made the important decisions: what to do about Jerusalem, whether China should be admitted to the United Nations, how to deal with crime in the streets. Economists are determined little-thinkers. They want to know what will happen to the production of houses and automobiles in 1968 if Congress votes a 10 percent surcharge on personal and corporate tax bills, and what will happen if Congress does not. They would like to be able to predict the course of the Wholesale Price Index and its components, and the total of corporate profits by in-

Galbraith Notes

11/7

Galbraith (forgot to print)

Stockholders have no power
but seems weakly written
like would have (and do have w/ enough votes)
but too difuse that no one really puts in the time
but w/ big ~~[illegible]~~ fights
- Disney
- others (I'm not good at examples)

Can force change

What system would be better?
Same w/ US democracy
Threat of it holds people accountable

7

~~Soll~~ Solon

reaction to Gailbraith

big thinkers vs little thinkers

1. Giant corps
2. Not run by stockholders

   Decisions in interlocking bureaucracy

   "technostructure"

3. Avoid risk

   finance itself out of retained earnings

   manages consumer to buy

   (this is an extream POV!)

4. Seeks survival, not profit

   fastest growth of sales

   ↑ dividend

   tech virtuosity (skill)

(3)

5. More things = happiness

6. key is organized intellegence
   sci + managerial

Modern capitalism has not come to terms w/ the modern corp

external financing not trivial ...

Consumer managed by Madison Ave

Response

My response is kinda disorganized (bad for GRE :))

11/7

Galbraith Reaction

Michael Plasmeier

I do not agree with Galbraith's assertion that stockholders have absolutely no control over corporations and that this is a bad thing.

First off, Galbraith points out that there have been points where large stockholders have influenced the direction of a company. However, much of the stock is owned by small stockholders. Individually these stockholders cannot change the outcome. But they may try to band together. However, even this is difficult, because the marginal input shareholders have is not worth the large amount of time and effort needed by each shareholder to plan business strategy. Instead, they entrust this to experts who have are dedicated full time to the problem.

They might not be able to pick the individual people, but if something goes wrong, they can make major changes. This incentivizes management to stay relatively (albeit not exactly) on target. If something is egregious enough to raise attention, the shareholders will react.

This is the same how politics works. Each voter does not research and decide every bill. However representatives know that their actions will be watched. If they do something egregious, then they will be voted out of office during the next election. We can see this happened when the state of PA legislature voted themselves a pay raise in the middle of the night.[1]

Even the legislator cannot review every action the executive branch takes. They set the ground rules through laws and if something goes wrong, they hold a hearing. This is the same function that the shareholders serve in a corporation. It is the right balance of accountability and efficiency.

---

[1] http://www.philly.com/philly/blogs/growls/Pay-Raise-Remembered.html

14.72 11/7

"I sent mix signals"

Summarize Polyani
Shumpter
Galibrath + Solow ∈ reading for ~~da~~ today

Polyani Commodity Markets through history

- L any object was sold

~~dea~~

* ⊛ But 19th century : organize whole economy/ Society around markets
  - land
  - labor
  - money

"Unnatural" - not how humans naturally live

② Due to

Ideas ; Libralism/Neoclassical

Like Weaber in that series of ideas creates structures of economy

Try to transform society through legislation

Creates markets

* Since unnatural → counter movement

Disrupts full effect of the market

Ossilation againts market → facism + communism

Yesterday's election ; another oscilation

Review

New

Gold standard

All $ backed by gold

; Cap on amt of $ in economy

③

$$GDP = \sum P_i Q_i \equiv Wages + Rent + \cdots + \Pi$$

<u>Quantity theory of money</u>

$$MV = GDP$$

amt of money = supply of gold

velocity of money = amt of times gold circulates in year

If velocity variable → get as much as you need

But we generally assume it is fixed by other things

$$\underbrace{M \cdot V}_{\text{if both fixed}} = \underbrace{P \cdot Q}_{\text{to expand economy prices have to go down}}$$

Usually we think of gold supply in world is fixed.

4

Trade other countries for gold

gold for goods

If can't sell enough goods to get the gold

↳ lower the price

Still in equalibium

But have deflation as prices ↓

If prices don't fall → unemployment

which accumulates

Then revolution / starvation

Polyani's argument Social pressures to make

prices fall are disruptive to society

So the deflation requires society to be shaken up

Having this all based on gold std would be painful

5

Greece can't sell enough goods in World Market
in order for them to maintain their consumption
esp. gov expenditures

~~Borrow~~
So its borrowing ~~$~~ € from German banks
Who ~~are~~ have € in ~~circulation~~ deposit

Prof: The € is functioning as ~~gold~~ gold

Can German banks always lent to Greece
Have they run out of Euros?
So pressure in Greece to lower prices
But prices are not falling enough

Unemployed angry → strike
might be revolution

(6)

One sol: leave Euro
(like leaving gold std)
but supply of $ controlled by Euro Central Bank
but ECB is not growing the $ supply

then world inflate Drachma to lower real pay
"devalue"

forcing rel prices down

Strict gold std → Gold is $ used
Limited by amt of gold
$ just a easier way than hauling gold

Banks can issue $
Trust when take it to bank, people will honor it
How do you build that faith?
Gold: Axiom trusted
$: Gov collects taxes - such a big buyer - is trusted

(2)

So on gold standard ; lots of pressure on
adjustments via prices
which don't adjust easily

Humans are bound in community
People don't do things just since prices say so

Why would unemployed not return to textile industry
"it would kill my grandparents"
Who worked very hard to escape that industry
They - individually - would
but since they live in society - it has
a meaning - would undermine that meaning

Europe today ; Mechanisms are the same
As Polanyi talked about

So why did they create the Euro in the
first place

8

Detroit

very high unemployment downtown

like Greece

So why having problems - sure

Detroit is part of US union

could solve problems if could devalue

but no ~~one~~ has ever mentioned this idea!

Since something more complicated

need std currency over some area

but what is the right ~~amount~~ amt

Polanyi: People went on gold std in 1920s

to facilitate int'l trade

and ~~xxx~~ since very bose central banks → inflation

(ie Germany 100 years ago)

9

Us went on Gold st after WWI

Then Great Depression ended it in US

Since close to producing a revolution

Actually caused communism in the US

New system: facilitate trade

<u>Betton Woods</u> fixed to $ kinda

abandoed 1970s

<u>Owenism</u>

- New answers what is sol

Suggestion what could be ans: Owenism

British Industrialist

Communal organization

Provided stability

Modeled on mideval closed community

(16)

Recipocity
Redistibution
Homesteading

Viewed as Utopian

Polayni: Could it be a way to organize a saiety
outside of market mechanism

Notion that protection takes place in community
↳ we will come back to
Last paper: Role of cooperation + community
in production

Last assignents for course: Soul of New Machine
Double Helix

Those are about systems of production not
soly on indv or market
But are modern / contempary

(11)

Some communal aspects
Like how Polanyi discusses Owenism
Discuss your cooperation ~~[illegible]~~ at MIT
Versus individual - faster to do a pset
yourself than w/ a group

Polanyi's Owenism

way to org society w/ cooperation + community
So pressures of gold std are disruptive
and types of relationships needed for
advanced/efficient economy

Schumpeter

important figure in Econ
└ in odd way
Very diff + original ideas
but all economists read him

⑫

Though might not agree

---

he mixes std economic theory w/ sociological theory

ideas have same inspiration as Weber + Polanyi

- humans are embedded in community
- humans are influenced by ideas

Not so easy to see how they are operating

important ideas in Schumpeter are not easy summarized

Schumpeter's Theory of Economic Growth

Steady State Equilibrium

- imagine a world that has settled down
- Circular flow

~~Phlon~~ Prof : each person specializes
but trades w/ others w/ prices

(13)

Economics: How you get to a central equilibrium of prices

Schumpeter: If settle into a steady state then prices are consistent w/ that
No need to worry about equilibrium → you've settled in to flow

Once Econ gets there: a world of little innovation and change

Economic =libium → Social =libium
~~the~~ Since people don't like elaborate change
Social pressures to be conservative and not change
Tech change / innovation comes into that world
↑ The entrepreneur
Prof: super ↑ fashionable today but Schumpeter introduced it

(14)

invention vs innovation

↑ all the time
not much credit
to inventor

↑ brings invention into social use
introduce innovation into daily life
break through barrier to change

Some Lone Wolf "Roarks" are willing to go againts this Conservative force of society

But not like Roark who is also an inventor

Schumpeter: invention is seperate, not really required

→ interrupts social ~~eq~~ equilibrium
Causes econ to expand
Causes ↑ flow of business Cycle

Once break through social innovation
lots of followers
Everyone has an iPhone clone now

(15)

eventually you get saturation

Then less investment

you fall back to depression

Until you get a new set of innovations

* must have <u>technological change</u>

---

he also produces theory of the <u>business cycle</u>

lots of <u>emphirical work</u>

---

also has theory on <u>long run evolution on econ</u>

Early stages of capitalism → entpreneurial system

Over time → capitalism evolves

in direction Marx and Weber saw it

innovation institutionalized in large firms

No longer dependence on entpreneurs

(16)

Econs evolve to Socialism

└ but ~~diff~~ reasons than Marx

Series of ideas connected w/ capitalism

Come back to bite + destroy capitalism

Rationalism + Pacifism

Will talk further in Next Class

as well as Galbraith + Solow

14.72 Capitalism and its Critics
Fall, 2012
Professor Michael Piore

Second Paper Assignment
Due November 9, 2012

Write a paper of 7-10 pages on the following subject.

Compare and contrast the work histories of two (or three) generations of your family and then interpret those histories in light of the different views of capitalism, and of the way it functions, which you have encountered thus far in the course.

You should feel free to organize this essay in a way that you find most interesting and revealing, but in the past most students have approached this problem in stages:

1. Interview knowledgeable members of your own family (typically your mother and grandmother or your father and grandfather) about their work histories (careers).

2. Think about your own work history thus far and how your career is likely to develop in the future.

3. Compare and contrast the three career trajectories.

4. Pick out one author from each of the three paradigms we have considered (liberalism, Marxism, and sociological), and outline their views about what determines the fate of individuals in the economy.

5. Discuss the ways in which those views do and do not seem to explain the similarities and differences in the career trajectories as you have laid them out in step 3.

You do not necessarily have to write this essay about your own family; you could interview members of another family. But it is generally easier to collect information on your family and more interesting for you as the writer (and me as the reader).

Paper 2
14.72

11/10

7-10 pgs

Compare + Contrast history of your family

Interpret it w/ diff views of capitalism + how it functions

include specific quotes from Authors

1. Interview families

Listen back to Grandmom

That was WW2

Could talk about German econom in general

2. Think about your work history

Did That today for a bunch of hrs!

Much more freedom

Grandmom - Bank Teller, very regimented

Mom - Nurse some discretion

Me: Much more discretion

2

3. Compare + Contrast Career trajectories

4. Pick an author + compare their views

Are these alt topics or all together?

5. Discuss how views do + don't explain similarities differences

~~Mom: Was~~

Grandma: Stay at home mom

Call Mom

Grand Mom - Stay at home

later as bank teller

father divorced

dry cleaners

Customer service

then bank

Grand dad - Could do anything

Blacksmith

3)

"Could do anything"

Had his own biz in village

Repaired stuff

Full time job: Factory

IDK what made

Wurtzburg

Later on: Cos to manage machinery

Wool co

Military Civilian

Technical Supervisor

for the base

heating + cooling system

(Me: Not a preset position)

(4)

Helped at people
Made friends easily
Helped them at
Fixed his laundry machine
~~@~~

Biz in house / yard
but outside
Welding

Both Mom + Dad didn't go to uni
Fields when ~~he~~ she little
Mom + Grandmom worked in fiel
Potatoes
Mom had to help

(5)

Another lands - mostly woods
Gardens

~~A~~ Basement next to house

4 chickens
Big barn
Mom climb up
Hid in straw

No heat
Just wood stove
Cooked on
(I'm more spoiled)

After the war in Germany after war
bought i meat, milk,
butter mom bought

6

Went to farmers themselves

dog ate bones + paper

Cream

└ make butter on sun

drank milk

└ not anymore

---

60 + 70s

life easier

had tv

1965 - got TV B+W

later got telephone

very expensive

made a lot of $

7

Stolte : Bundes post
All run by state
Then went under/changed

6-7 years old - hat store
Walked far to see
kinder from Bia byo
Watch Biller-bir
Could walk around

My Dad - didn't hear from him

Ok how to organize paper:
tell each generations story
↳ then analize after each

8

Well in the other presented

Sounds good

---

do opening last

or cold open

; how much analysis to mix in

; or keep sep

prob best to mix it in...

Unless what common themes

Now I need to look at authors

privitization - Friedman

L kinda

SOE

(9)

Small biz: Friedman

Work ethic -> from my mom

└ Weber
bt not protestanism

Privitization -> Polayni

└ liked the collectivism
not the everyone man for themself

bounce b/w state supporters

My mom didn't agree

└ thought state was worse

Shumpeter -> the entprenure
brings change
(me)

(10)

Or me like a Rock
w/o the individualism...

Shumpeter i creative destruction

Shows my limited/surface analysis
since I didn't super closely read those...)
And have trouble remembering
And lazy to look up...

I write in a very plain style
(How was I taught in style in HS?

I don't speak much about WWI + post WW2
Lsince my source (mom) had no insights

This class doesn't really teach the standards of analysis
↳ unlike the previous one

(11)

Discuss the ways in which those views do or do not seem to explain the similarities + differences in career trajectories.

I didn't quite do that

? Meta level of analysis

I don't get how people can write pages + pages on this stuff!

Fate of individuals

That is summary

? One more orthodox list?

Work ethic

Keynes?

he was gov investment

labor not go down

People save

(12)

Stumbled on a good comparison!

Draft 1

11/11
2:30A

Essay 2
Three Generations

Michael Plasmeier

My Grandmom

before, during, and after WW2

My grandmom and grandfather (on my mother's side) lived in Germany. ~~My grandmom was born around 1930, meaning she lived through World W~~ar II. Before and during the war, supplies were sparse as Germany was going through much economic change.

Date

My mom was born in 1952, in the immediate post war period. The family originally had a small farm, where they grew potatoes, among other crops. for personal use ~~My mom remembers hiding in the hay in the barn.~~ They also had a small garden on the property. They kept a few chickens. They didn't buy much: only meat and milk. Those were sold by farmers in the local village. There was not even a formal "market area" like you might find today. They didn't have much comfort at home, only a wooden stove.

Later on, in 1965 they got a black and white television. But they still did not have a telephone. When they finally got one, it was very expensive because it was run by a government-owned monopoly. In Germany, telephone service was run by the state-owned monopoly Deutsche Bundespost (the Post Office) until privatization in 1996.

in her life

My grandmom originally stayed at home and took care of the children. Later on, when she divorced my grandfather, she ~~got~~ started working ~~had to get~~ a job on her own. She worked for some time as a clerk in a dry cleaner. After that, she was a teller at a bank.

My grandfather was an iron worker and a mechanic. Early on, when my mom was little, he had a small business where he would repair items for the local village. He worked in the yard outside of house, ~~sometimes welding~~ repairing. He also had a full time job working in ~~the~~ a factory ~~at the same time.~~ When the family moved to a new town, he fixed ~~the~~ machinery in a wool factory. At the end of his career, he was a technical supervisor of building systems (for example, heating and cooling) for ~~the~~ a nearby military base. He still continued to work on the side to fix things for people. For example, he would fix laundry machines at the local Laundromat.

Both of them did not attend university. keep

My Mom and Dad

My mom is a nurse at Main Line Health, a local health care conglomerate. She drives around and visits patients who live in their own homes. She has some discretion in this job. Unlike my grandmom and grandfather who clocked in and out when they worked, my mom is on salary. She can decide what time and in what order to visit patients. No one is measuring how long she stopped for lunch.

~~Most~~ Many of her patients are on Medicare and Medicaid, which are government-sponsored health care programs. However, the company she works for is privately owned and has some non-government patients as well.

My dad is a television repairman who owns his own small business. It's a sole proprietorship and he is the only employee, save for sometimes my brother and I. He runs it out of our house. It's a ~~business~~ an industry that has been declining, but my dad sticks with it since he can't find other work. It makes up a very small percentage of our household income (5-10%).

My mom went university and then graduated from nursing school. My dad left school right before getting his teaching degree. This is more edu than my Grandparents - but only my mother is putting it to use, ~~in the fi~~ working directly in the field she studied when she was little

We live much differently than my mom did ~~growing~~ up. We live in a typical American suburb of Philadelphia. We are middle class, in the 75th percentile of income in the US. We have all the comforts of home, including a speedy internet connection and a large screen TV.

Me

Past

publically owned

gov owned and privately owned

I've worked at both large and small companies. In high school, I started my own company called SocialView. I had one of the top 100 apps on Facebook back in 2007-2008. At the time it was just me and a partner I brought own to invest in the app and provide advice. I made a few thousand $ off it.

One I was my own bit

Freshmen summer, I worked at Deutsche Bahn, the German national railway. It's fairly well run, but it's still 100% Government owned. Today it is facing mandated competition from other ~~railroads~~ railroads. The government is mandating that it leases out its tracks to other train operating companies. In addition, it needs to bid ~~to regional governments in order~~ against these upstarts for regional contracts to offer subsidized regional services. At the start of next year, bus companies will begin to be able to compete with Deutsche Bahn to offer services.[1]

a publically owned global entertainment conglomerate

Last summer I worked at Disney. Disney showed me what a large ~~privately owned~~ company is like. ~~It is~~ In some way not all that different from Deutsche Bahn. With so many things going on at once, it is hard to get them all to mesh together ~~well~~ efficiently.

I've also worked at midsized companies (those with about 100 employees). They seemed a lot more focused and a lot less complex than the large companies

~~non gov~~

---

[1] http://www.dw.de/green-light-for-long-distance-buses-in-germany/a-16352871

I've also worked doing small projects on contract for others. In some ways, this is like my father and grandfather who ran small businesses on the side to do odd-jobs for others.

Future

I am currently looking for a job. It's been difficult because what I have to offer is not exactly standard. I'm looking for a company that would be a good match for the skills I have. That position is probably not one that they have posted online. At the large places I've worked: Deutsche Bahn and Disney, I have not worked at one of their standard jobs. Interesting enough at both of the medium size places (~100 employees each), I have worked a standard role.

And in any case, I haven't and I won't be doing the same thing over and over again all day. As an analyst or as a product manager every day is completely different and faces new challenges. To some extent, projects will wind down and new ones will start up that were similar to the last. However, especially at a small company in the tech world, the company and the market are growing and changing so fast that one can't fall into a standard pattern.

And I'll be judged on hitting macro targets – what does the finished product look like and did it reach the goals I set. No one will be counting my hours or some micro view of my schedule (ie, how many meetings I had that day).

In fact, I am likely to start my own firm someday. In some ways this is like my father and grandfather, but it would not be just a job-shop, but a growth start up. Here I would have almost complete control about what I do. Unless I took investors, in which case they would tell me what to do. But they would do so at a super macro level – with quarterly board meetings.

Economics

Small Business: Friedman

All three generations of my family have run their own small businesses on the side to provide incremental income. Milton Friedman would have loved this. All three generations were able to see a small hole in the market and fill a need. There were no complicated governing structure, or government incentives, or regulations – just ~~generations of people earning~~ families individuals making money on the side selling their time on the open market for supplemental income.

Weber: Separate Business Realms

My business, my father's business, and my grandfather's business have all been run out of ~~our~~ their homes. That is not true capitalism as under Weber. Under Weber, Capitalism requires something more – it requires a real quest for, what I would call, a growth business. Growth businesses ~~on the other hand~~ are those where the owner hopes that the prospects for future growth mean that the business will be worth more than just its current cash flows and liabilities. Many small businesses in the US are lifestyle businesses. They are run as ~~either~~ the main income for the family. For example: a family that operates a local restaurant. The family has no real intensions of growing the business – they just ~~take~~ use the profits to feed their families. These profits are fairly standard over the long run. Hobby businesses, such as the ones ~~I described above,~~ my family has had, are just on the side for a little extra spending money. Weber exempted these types of business from capitalism.

a way to organize work

Privatization: Polanyi

My stories in Germany cover the trend of the increasing privatization of firms. Polanyi spoke about liberalism as an ideology, which created the institutions required for capitalism. He probably would have predicted the widespread liberalism ideology which gripped much of Europe in the 80s and 90s. And led to the privitization of many State-owned ~~German~~ firms.

However, both my mother and I ~~spoke~~ speak positively about privatization. My mother spoke about her very expensive goverment - monopoly - provided telephone line as a child. Privatization ended up cutting telephone rates drastically. ~~Plus~~ When I worked at Deutsche Bahn, I saw a lot of seeming inefficiency. It could just be that I did not understand the language well enough, but there seemed to be a good amount of paper shuffling, as well as policies and procedures. ~~Certainly the division where I worked was forward thinking.~~ Tho I saw a company in transition into one that had to be a lot more responsive to the market.

Did the privatization of these state-owned monopolies hurt the community? I would argue no – Germany has grown stronger because these systems are just more efficient and the companies are more responsive to the needs of consumers.

The Entrepreneur: Schumpeter

In the future I see myself being an entrepreneur. ~~I'm likely to be more of~~ an innovator ~~than an inventor in~~ and as Schumpeter~~'s terms~~ defines ~~it~~ them. I want to change things. I want to work at firms which are revolutionizing industries. This is what is exciting and interesting to me. Things staying the same are boring.

That is a huge change from my mom and grandmom who worked in standard positions inside large companies. In their roles, they worked under a specific job title and job description. My mom does the same thing all day – just with different patients. ~~Now every patient is different, and that is what makes the job intellectually challenging~~ She has more discretion than my Grandmom, however the work is still pretty similar all day.

Even my father and grandfather, who worked on their own, worked inside existing conventions and roles. You could find someone doing their ~~role~~ job in every town and village. The firms that I would join, or start my own thing in, would all look beyond the immediate town the company is based in. All would ~~be aiming for a~~ national impact. growth businesses seeking to revolutionize industries I think we are still too far away from being able to have an international impact. Perhaps my children will be able to start something that is recognized internationally. The internet has allowed media to spread internationally. I can read a British newspaper online, instead of an American one. This grows the shared, cross-border culture making it easier for business to work internationally.

I wonder how this will affect the world. As more people become national-focused entrepreneurs, will we still have local ~~entrepreneurs~~ businesses? Will we have the little stores that my mom shopped at as a girl? Or will she shop at Real-, a German equivalent of Wal-Mart? In fact, my advisor Prof. Brynjolfsson tries to address this in his book Race against the Machine: How the Digital Revolution is Accelerating Innovation, Driving Productivity, and Irreversibly Transforming Employment and the Economy.

Will we even have standard jobs?

Weber: Work Ethic

I think I learned my work ethic from my mom. She works hard every single day to support her family. She also insisted that I do my homework with the same passion~~s~~ for completion + accuracy since early elementary school. This has given me implicit motivation. I want to get things done and do a good job not because I want to make the most money or because I believe in a God that ordains work, but because of something else. I don't know how to define it, but there seems to be some characteristics Germans share that include their desires for quality, as well as their love for policies and procedures.

This naturally leads into the Capitalist Spirit, much like Ben Franklin.

The Fate of Individuals

meh

Over time the fate of ~~individuals in my story have been~~ somewhat consistent and somewhat different. ~~All worked in~~ times of general capitalism. But as time as gone on, Services that were once protected government monopolies are being opened to competition. Capitalism grows stronger.

Plus more freedom, more discretion

Whereas each generation of my family has had their own hobby business, I look to build a real growth business, consistent with Schumpeter's definition. I might be the first to work without a preexisting job description. And I will likely have the most discretion in my work than anyone before me. Instead of monitoring small things like the hours I work, I will be judged by the results I deliver.

Individualism was strong throughout the 3 generations of my family

Standards of living are rising, and will continue to rise. I will likely make just about, or even slightly more than both of my parents combined right out of school.

I think it is an exciting time and an interesting progression to have.

Polyani thinks we might swing back
But Obama has been pretty center
and might move even more centrist
w/ this recent change

11/11
4PM

~~procedures. This naturally leads into the Capitalist Spirit, much like Ben Franklin was also driven by something else inherent in him.~~

2nd draft - just conclusion

The Fate of Individuals

Individualism ~~was~~ has been strong throughout the three generations of my family. All worked in times of the generations general capitalism. But as time as gone on, capitalism grows stronger. Services that were once protected as ~~protected~~ government monopolies were opened to competition. Plus, workers had more discretion, as they moved from being judged by a time clock to meeting macro goals. ~~Instead of monitoring small things like the hours I work,~~ I will be judged by the results I deliver, not the hours I work. Jobs also have had more discretion and are more open ended, than the previous generations narrowly defined jobs. I might be the first in my family to work without a preexisting job description. Individuals in the past in my family have run hobby businesses, but I seek to build a real growth business, consistent with Schumpeter's definition. In addition, standards of living are rising, and will continue to rise. I will likely make just about, or even slightly more than both of my parents combined right out of school.

I think it is an exciting time and an interesting progression to have. Polanyi might be think we will swing back to less market control, but I think this is unlikely to happen. Obama has been pretty centrist, and is likely to move even more centrist with the recent election.

It is interesting to think a

tense

Final

11/11 (extension to 11/12)

Essay 2
Three Generations

Michael Plasmeier

My Grandmom

My grandmom and grandfather (on my mother's side) lived in Germany before during and after World War II.[1] Before and during the war, supplies were sparse as Germany was going through much economic change.

My mom was born in 1952, in the immediate post war period. The family originally had a small farm, where they grew potatoes, among other crops for personal use. They also had a small garden on the property. They kept a few chickens. They didn't buy much: only meat and milk. Those were sold by farmers in the local village. There was not even a formal "market area" like you might find today. They didn't have much comfort at home, only a wooden stove.

Later on, in 1965 they got a black and white television. But they still did not have a telephone. When they finally got one, it was very expensive because it was run by a government-owned monopoly. In Germany, telephone service was run by the state-owned monopoly Deutsche Bundespost (the Post Office) until privatization in 1996.

My grandmom originally stayed at home and took care of the children. Later on in her life, when she divorced my grandfather, she started working on her own. She worked for some time as a clerk in a dry cleaner. After that, she was a teller at a bank.

---

[1] Personal interview with my mom conducted 11/10/2012

My grandfather was an iron worker and a mechanic. Early on, when my mom was little, he had a small business where he would repair items for the local village. He worked in the yard outside of house. He also had a full time job working in a factory at the same time. When the family moved to a new town, he fixed machinery in a wool factory. At the end of his career, he was a technical supervisor of building systems (for example, heating and cooling) for a nearby military base. He still continued to work on the side to fix things for people. For example, he would fix laundry machines at the local Laundromat.

Both of them did not attend university.

My Mom and Dad

My mom is a nurse at Main Line Health, a local health care conglomerate. She drives around and visits patients who live in their own homes. She has some discretion in this job. Unlike my grandmom and grandfather who clocked in and out when they worked, my mom is on salary. She can decide what time and in what order to visit patients. No one is measuring how long she stopped for lunch.

Many of her patients are on Medicare and Medicaid, which are government-sponsored health care programs. However, the company she works for is privately owned and has some non-government patients as well.

My dad is a television repairman who owns his own small business. It's a sole proprietorship and he is the only employee, save for sometimes my brother and I. He runs it out of our house. It's an industry that has been declining, but my dad sticks with it since he can't find other work. It makes up a very small percentage of our household income (5-10%).

My mom went university and then graduated from nursing school. My dad left school right before getting his teaching degree. This is more education than my grandparents received. Still only my mom is working in the field in which she received her degree.

We live much differently than my mom when she was growing up. We live in a typical American suburb of Philadelphia. We are middle class, in the 75^{th} percentile of income in the US. We have all the comforts of home, including a speedy internet connection and a large screen TV.

Me

Past

I've worked at both large and small companies, government owned, publically owned, privately owned, and personally owned. In high school, I started my own company called SocialView. I had one of the top 100 apps on Facebook back in 2007-2008. At the time it was just me and a partner I brought own to invest in the app and provide advice. I made a few thousand dollars off of it, which is not much in the scheme of things, but respectable for a high school student.

Freshmen summer, I worked at Deutsche Bahn, the German national railway. It's fairly well run, but it's still 100% Government owned. Today it is facing mandated competition from other railroads. The government is mandating that it leases out its tracks to other train operating companies. In addition, it needs to bid against these upstarts for regional government contracts to offer subsidized regional services. At the start of next year, bus companies will begin to be able to compete with Deutsche Bahn to offer services.[2]

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[2] http://www.dw.de/green-light-for-long-distance-buses-in-germany/a-16352871

Last summer I worked at Disney a publically owned, global, entertainment conglomerate. Disney showed me what a large privately owned company is like. In some ways it is not all that different from Deutsche Bahn. With so many things going on at once, it is hard to get them all to mesh together efficiently.

I've also worked at midsized companies (those with about 100 employees). They seemed a lot more focused and a lot less complex than large companies.

I've also worked doing small projects on contract for others. In some ways, this is like my father and grandfather who ran small businesses on the side to do odd-jobs for others.

Future

I am currently looking for a job. It's been difficult because what I have to offer is not exactly standard. I'm looking for a company that would be a good match for the skills I have. That position is probably not one that they have posted online.

And in any case, I haven't and I won't be doing the same thing over and over again all day. As an analyst or as a product manager every day is completely different and faces new challenges. To some extent, projects will wind down and new ones will start up that were similar to the last. However, especially at a small company in the tech world, the company and the market are growing and changing so fast that one can't fall into a standard pattern.

And I'll be judged on hitting macro targets – what does the finished product look like and did it reach the goals I set. No one will be counting my hours or some micro view of my schedule (ie. how many meetings I had that day).

In fact, I am likely to start my own firm someday. In some ways this is like my father and grandfather, but it would not be just a job-shop, but a growth start up. Here I would have almost complete control about what I do. Unless I took investors, in which case they would tell me what to do. But they would do so at a super macro level – with quarterly board meetings.

Analysis: Through the Lens

Small Business: Friedman

All three generations of my family have run their own small businesses on the side to provide incremental income. Milton Friedman would have loved this. All three generations were able to see a small hole in the market and fill a need. There was no complicated governing structure, or government incentives, or regulations – just individuals making money on the side, selling their time on the open market for supplemental income.

Weber: Separate Business Realms

My business, my father's business, and my grandfather's business have all been run out of their homes. That is not true capitalism as under Weber. Under Weber, capitalism requires something more – it requires a real quest for, what I would call, a growth business. Growth businesses are those where the owner hopes that the prospects for future growth mean that the business will be worth more than just its current cash flows and liabilities. Many small businesses in the US are lifestyle businesses. They are run as the main income for the family. For example: a family that operates a local restaurant. The family has no real intensions of growing the business – they just use the profits to feed their families. These profits are fairly flat over the long run. Hobby businesses, such as the ones my family has had, are just a way to organize work on the side for a little extra spending money. Weber exempted these types of business from capitalism.

Privatization: Polanyi

My stories in Germany cover the trend of the increasing privatization of firms. Polanyi spoke about liberalism as an ideology, which created the institutions required for capitalism. He probably would have predicted the widespread liberalism ideology which gripped much of Europe in the 80s and 90s and led to the privatization of many state-owned firms.

However, both my mother and I speak positively about privatization. My mother spoke about her very expensive government-monopoly-controlled telephone line as a child. Privatization ended up cutting telephone rates drastically in Germany and elsewhere. When I worked at Deutsche Bahn, I saw a company in transition from a large bureaucracy to one that had to be a lot more responsive to the market.

Did the privatization of these state-owned monopolies hurt the community? I would argue no – Germany has grown stronger because these systems are just more efficient and the companies are more responsive to the needs of consumers.

The Entrepreneur: Schumpeter

In the future I see myself being an entrepreneur and innovator as Schumpeter defines those terms. I want to change things. I want to work at firms which are revolutionizing industries. This is what is exciting and interesting to me. Things that stay the same are boring.

That is a huge change from my mom and grandmom who worked in standard positions inside large companies. In their jobs, they worked under a specific job title and job description. My mom does the same thing all day – just with different patients. Now every patient is different, and that is what makes the job intellectually challenging, however the work is pretty similar all day.

Even my father and grandfather, who worked on their own, worked inside existing conventions and roles. You could find someone doing their role in every town and village. The firms that I would join, or start my own thing in, would all look beyond the immediate town the company is based in. All would be a national impact growth business seeking to revolutionize industries.

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Essay 2
Three Generations

Michael Plasmeier

My Grandmom

My grandmom and grandfather (on my mother's side) lived in Germany before during and after World War II.[1] Before and during the war, supplies were sparse as Germany was going through much economic change.

My mom was born in 1952, in the immediate post war period. The family originally had a small farm, where they grew potatoes, among other crops for personal use. They also had a small garden on the property. They kept a few chickens. They didn't buy much: only meat and milk. Those were sold by farmers in the local village. There was not even a formal "market area" like you might find today. They didn't have much comfort at home, only a wooden stove.

Later on, in 1965 they got a black and white television. But they still did not have a telephone. When they finally got one, it was very expensive because it was run by a government-owned monopoly. In Germany, telephone service was run by the state-owned monopoly Deutsche Bundespost (the Post Office) until privatization in 1996.

My grandmom originally stayed at home and took care of the children. Later on in her life, when she divorced my grandfather, she started working on her own. She worked for some time as a clerk in a dry cleaner. After that, she was a teller at a bank.

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[1] Personal interview with my mom conducted 11/10/2012

My grandfather was an iron worker and a mechanic. Early on, when my mom was little, he had a small business where he would repair items for the local village. He worked in the yard outside of house. He also had a full time job working in a factory at the same time. When the family moved to a new town, he fixed machinery in a wool factory. At the end of his career, he was a technical supervisor of building systems (for example, heating and cooling) for a nearby military base. He still continued to work on the side to fix things for people. For example, he would fix laundry machines at the local Laundromat.

Both of them did not attend university.

My Mom and Dad

My mom is a nurse at Main Line Health, a local health care conglomerate. She drives around and visits patients who live in their own homes. She has some discretion in this job. Unlike my grandmom and grandfather who clocked in and out when they worked, my mom is on salary. She can decide what time and in what order to visit patients. No one is measuring how long she stopped for lunch.

Many of her patients are on Medicare and Medicaid, which are government-sponsored health care programs. However, the company she works for is privately owned and has some non-government patients as well.

My dad is a television repairman who owns his own small business. It's a sole proprietorship and he is the only employee, save for sometimes my brother and I. He runs it out of our house. It's an industry that has been declining, but my dad sticks with it since he can't find other work. It makes up a very small percentage of our household income (5-10%).

My mom went university and then graduated from nursing school. My dad left school right before getting his teaching degree. This is more education than my grandparents received. Still only my mom is working in the field in which she received her degree.

We live much differently than my mom when she was growing up. We live in a typical American suburb of Philadelphia. We are middle class, in the 75^{th} percentile of income in the US. We have all the comforts of home, including a speedy internet connection and a large screen TV.

Me

Past

I've worked at both large and small companies, government owned, publically owned, privately owned, and personally owned. In high school, I started my own company called SocialView. I had one of the top 100 apps on Facebook back in 2007-2008. At the time it was just me and a partner I brought own to invest in the app and provide advice. I made a few thousand dollars off of it, which is not much in the scheme of things, but respectable for a high school student.

Freshmen summer, I worked at Deutsche Bahn, the German national railway. It's fairly well run, but it's still 100% Government owned. Today it is facing mandated competition from other railroads. The government is mandating that it leases out its tracks to other train operating companies. In addition, it needs to bid against these upstarts for regional government contracts to offer subsidized regional services. At the start of next year, bus companies will begin to be able to compete with Deutsche Bahn to offer services.[2]

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[2] http://www.dw.de/green-light-for-long-distance-buses-in-germany/a-16352871

Last summer I worked at Disney a publically owned, global, entertainment conglomerate. Disney showed me what a large privately owned company is like. In some ways it is not all that different from Deutsche Bahn. With so many things going on at once, it is hard to get them all to mesh together efficiently.

I've also worked at midsized companies (those with about 100 employees). They seemed a lot more focused and a lot less complex than large companies.

I've also worked doing small projects on contract for others. In some ways, this is like my father and grandfather who ran small businesses on the side to do odd-jobs for others.

Future

I am currently looking for a job. It's been difficult because what I have to offer is not exactly standard. I'm looking for a company that would be a good match for the skills I have. That position is probably not one that they have posted online.

And in any case, I haven't and I won't be doing the same thing over and over again all day. As an analyst or as a product manager every day is completely different and faces new challenges. To some extent, projects will wind down and new ones will start up that were similar to the last. However, especially at a small company in the tech world, the company and the market are growing and changing so fast that one can't fall into a standard pattern.

And I'll be judged on hitting macro targets – what does the finished product look like and did it reach the goals I set. No one will be counting my hours or some micro view of my schedule (ie. how many meetings I had that day).

In fact, I am likely to start my own firm someday. In some ways this is like my father and grandfather, but it would not be just a job-shop, but a growth start up. Here I would have almost complete control about what I do. Unless I took investors, in which case they would tell me what to do. But they would do so at a super macro level – with quarterly board meetings.

Analysis: Through the Lens

Small Business: Friedman

All three generations of my family have run their own small businesses on the side to provide incremental income. Milton Friedman would have loved this. All three generations were able to see a small hole in the market and fill a need. There was no complicated governing structure, or government incentives, or regulations – just individuals making money on the side, selling their time on the open market for supplemental income.

Weber: Separate Business Realms

My business, my father's business, and my grandfather's business have all been run out of their homes. That is not true capitalism as under Weber. Under Weber, capitalism requires something more – it requires a real quest for, what I would call, a growth business. Growth businesses are those where the owner hopes that the prospects for future growth mean that the business will be worth more than just its current cash flows and liabilities. Many small businesses in the US are lifestyle businesses. They are run as the main income for the family. For example: a family that operates a local restaurant. The family has no real intensions of growing the business – they just use the profits to feed their families. These profits are fairly flat over the long run. Hobby businesses, such as the ones my family has had, are just a way to organize work on the side for a little extra spending money. Weber exempted these types of business from capitalism.

Privatization: Polanyi

My stories in Germany cover the trend of the increasing privatization of firms. Polanyi spoke about liberalism as an ideology, which created the institutions required for capitalism. He probably would have predicted the widespread liberalism ideology which gripped much of Europe in the 80s and 90s and led to the privatization of many state-owned firms.

However, both my mother and I speak positively about privatization. My mother spoke about her very expensive government-monopoly-controlled telephone line as a child. Privatization ended up cutting telephone rates drastically in Germany and elsewhere. When I worked at Deutsche Bahn, I saw a company in transition from a large bureaucracy to one that had to be a lot more responsive to the market.

Did the privatization of these state-owned monopolies hurt the community? I would argue no – Germany has grown stronger because these systems are just more efficient and the companies are more responsive to the needs of consumers.

The Entrepreneur: Schumpeter

In the future I see myself being an entrepreneur and innovator as Schumpeter defines those terms. I want to change things. I want to work at firms which are revolutionizing industries. This is what is exciting and interesting to me. Things that stay the same are boring.

That is a huge change from my mom and grandmom who worked in standard positions inside large companies. In their jobs, they worked under a specific job title and job description. My mom does the same thing all day – just with different patients. Now every patient is different, and that is what makes the job intellectually challenging, however the work is pretty similar all day.

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I don't really see an alternative here - isn't state interference compatible with international competition?