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Capitalism, Socialism and Democracy

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PROLOGUE

CAN capitalism survive? No. I do not think it can. But this opinion of mine, like that of every other economist who has pronounced upon the subject, is in itself completely uninteresting. What counts in any attempt at social prognosis is not the Yes or No that sums up the facts and arguments which lead up to it but those facts and arguments themselves. They contain all that is scientific in the final result. Everything else is not science but prophecy. Analysis, whether economic or other, never yields more than a statement about the tendencies present in an observable pattern. And these never tell us what *will* happen to the pattern but only what *would* happen if they continued to act as they have been acting in the time interval covered by our observation and if no other factors intruded. "Inevitability" or "necessity" can never mean more than this.

What follows must be read with that proviso. But there are other limitations to our results and their reliability. The process of social life is a function of so many variables, many of which are not amenable to anything like measurement that even mere diagnosis of a given state of things becomes a doubtful matter quite apart from the formidable sources of error that open up as soon as we attempt prognosis. These difficulties should not be exaggerated, however. We shall see that the dominant traits of the picture clearly support certain inferences which, whatever the qualifications that may have to be added, are too strong to be neglected on the ground that they cannot be proved in the sense in which a proposition of Euclid's can.

One more point before we start. The thesis I shall endeavor to establish is that the actual and prospective performance of the capitalist system is such as to negative the idea of its breaking down under the weight of economic failure, but that its very success undermines the social institutions which protect it, and "inevitably" creates conditions in which it will not be able to live and which strongly point to socialism as the heir apparent. My final conclusion therefore does not differ, however much my argument may, from that of most socialist writers and in particular from that of all Marxists. But in order to accept it one does not need to be a socialist. Prognosis does not imply anything about the desirability of the course of events that one predicts. If a doctor predicts that his patient will die presently, this does not mean that he desires it. One may hate socialism or at least look upon it with cool criticism, and yet foresee its advent. Many conservatives did and do.

Nor need one accept this conclusion in order to qualify as a socialist. One may love socialism and ardently believe in its economic, cultural and ethical superiority but nevertheless believe at the same time that capitalist society does not harbor any tendency toward self-destruction. There are in fact socialists who believe that the capitalist order is gathering strength and is entrenching itself as time goes on, so that it is chimerical to hope for its breakdown.

CHAPTER V

THE RATE OF INCREASE OF TOTAL OUTPUT

THE atmosphere of hostility to capitalism which we shall have to explain presently makes it much more difficult than it otherwise would be to form a rational opinion about its economic and cultural performance. The public mind has by now so thoroughly grown out of humor with it as to make condemnation of capitalism and all its works a foregone conclusion—almost a requirement of the etiquette of discussion. Whatever his political preference, every writer or speaker hastens to conform to this code and to emphasize his critical attitude, his freedom from "complacency," his belief in the inadequacies of capitalist achievement, his aversion to capitalist and his sympathy with anti-capitalist interests. Any other attitude is voted not only foolish but anti-social and is looked upon as an indication of immoral servitude. This is of course perfectly natural. New social religions will always have that effect. Only it does not make it easier to fulfill the analyst's task: in 300 A.D. it would not have been easy to expound the achievements of ancient civilization to a fervent believer in Christianity. On the one hand, the most obvious truths are simply put out of court *a limine*;[1] on the other hand, the most obvious misstatements are borne with or applauded.

A first test of economic performance is total output, the total of all the commodities and services produced in a unit of time—a year or a quarter of a year or a month. Economists try to measure variations in this quantity by means of indices derived from a number of series representing the output of individual commodities. "Strict logic is a stern master, and if one respected it, one would never construct or use any production index,"[2] for not only the material and the technique of constructing such an index, but the very concept of a total output of different commodities produced in ever-changing proportions, is a highly doubtful matter.[3] Nevertheless, I believe that this device is sufficiently reliable to give us a general idea.

[1] There is however another method of dealing with obvious though uncomfortable truth, viz., the method of sneering at its triviality. Such a sneer will serve as well as a refutation would, for the average audience is as a rule perfectly unaware of the fact that it often covers the impossibility of denial—a pretty specimen of social psychology.

[2] A. F. Burns, *Production Trends in the United States Since 1870*, p. 262.

[3] We cannot enter into this problem here. A little will, however, be said about it when we meet it again in the next chapter. For a fuller treatment see my book on *Business Cycles*, ch. ix.

For the United States, individual series good and numerous enough to warrant construction of such an index of output are available since the Civil War. Choosing what is known as the Day-Persons index of total production[4] we find that, from 1870 to 1930, the average annual rate of growth was 3.7 per cent and, in the division of manufactures alone, 4.3 per cent. Let us concentrate on the former figure and try to visualize what it means. In order to do this we must first apply a correction: since the durable equipment of industry was always increasing in relative importance, output available for consumption cannot have increased at the same rate as total production. We must allow for that. But I believe that an allowance of 1.7 per cent is ample;[5] thus we arrive at a rate of increase in "available output" of 2 per cent (compound interest) per year.

Now suppose that the capitalist engine keeps on producing at that rate of increase for another half century starting from 1928. To this assumption there are various objections which will have to be noticed later on, but it cannot be objected to on the ground that in the decade from 1929 to 1939 capitalism had already failed to live up to that standard. For the depression that ran its course from the last quarter of 1929 to the third quarter of 1932 does not prove that a secular break has occurred in the propelling mechanism of capitalist production because depressions of such severity have repeatedly occurred—roughly once in fifty-five years—and because the effects of one of them—the one from 1873 to 1877—are taken account of in the annual average of 2 per cent. The subnormal recovery to 1935, the subnormal prosperity to 1937 and the slump after that are easily accounted for by the difficulties incident to the adaptation to a new fiscal policy, new labor legislation and a general change in the attitude of government to private enterprise all of which can, in a sense to be defined later, be distinguished from the working of the productive apparatus as such.

Since misunderstandings at this point would be especially undesirable, I wish to emphasize that the last sentence does not in itself imply either an adverse criticism of the New Deal policies or the proposition—which I do believe to be true but which I do not need just now—that policies of that type are in the long run incompatible with the effective working of the system of private enterprise. All I now mean to imply is that so extensive and rapid a change of the social scene naturally affects productive performance for a time, and so much the most ardent New Dealer must *and also can* admit. I for one do not see how it would otherwise be possible to account for the

[4] See W. M. Persons, *Forecasting Business Cycles*, ch. xi.

[5] That allowance is in fact absurdly large. See also Professor F. C. Mill's estimate of 3.1 per cent for the period 1901-1913, and of 3.8 per cent for the period 1922-1929 (construction excluded; *Economic Tendencies in the United States*, 1932).

fact that this country which had the best chance of recovering quickly was precisely the one to experience the most unsatisfactory recovery. The only somewhat similar case, that of France, supports the same inference. It follows that the course of events during the decade from 1929 to 1939 does not *per se* constitute a valid reason for refusing to listen to the argument in hand which, moreover, may in any case serve to illustrate the meaning of past performance.

Well, if from 1928 on available production under the conditions of the capitalist order continued to develop as it did before, i.e., at a long-run average rate of increase of 2 per cent per year, it would after fifty years, in 1978, reach an amount of roughly 2.7 (2.6916) times the 1928 figure. In order to translate this into terms of average real income *per head of population*, we first observe that our rate of increase in total output may be roughly equated to the rate of increase in the sum total of private money incomes available for consumption,[6] corrected for changes in the purchasing power of the consumers' dollars. Second, we must form an idea about the increase in population we are to expect; we will choose Mr. Sloane's estimate, which gives 160 millions for 1978. Average income per head during those fifty years would therefore increase to a little more than double its 1928 amount, which was about $650, or to about $1300 *of 1928 purchasing power.*[7]

Perhaps some readers feel that a proviso should be added about the distribution of the total monetary income. Until about forty years ago, many economists besides Marx believed that the capitalist process tended to change relative shares in the national total so that the obvious inference from our average might be invalidated by the rich growing richer and the poor growing poorer, at least relatively. But there is no such tendency. Whatever may be thought of the statistical measures devised for the purpose, this much is certain: that the structure of the pyramid of incomes, expressed in terms of money, has not greatly changed during the period covered by our material

[6] "Consumption" includes the acquisition of durable consumers' goods such as motor cars, refrigerators and homes. We do not distinguish between transient consumers' goods and what is sometimes referred to as "consumers' capital."

[7] That is to say, average real income per head would increase at a compound interest rate of 1⅜ per cent. It so happens that in England, during the century preceding the First World War, real income per head of population increased at almost exactly that rate (see Lord Stamp in *Wealth and Taxable Capacity*). No great confidence can be placed in this coincidence. But I think it serves to show that our little calculation is not wildly absurd. In Number 241 of the *National Industrial Conference Board Studies*, Table I, pp. 6 and 7, we find that "per capita realized national income" adjusted by the Federal Reserve Bank of New York and the National Industrial Conference Board cost of living index, was in 1929 a little over four times the 1829 figure—a similar result, though open to still more serious doubts as to reliability.

—which for England includes the whole of the nineteenth century[8]—and that the relative share of wages plus salaries has also been substantially constant over time. There is, so long as we are discussing what the capitalist engine might do if left to itself, no reason to believe that the distribution of incomes or the dispersion about our average would in 1978 be significantly different from what it was in 1928.

One way of expressing our result is that, if capitalism repeated its past performance for another half century starting with 1928, this would do away with anything that according to present standards could be called poverty, even in the lowest strata of the population, pathological cases alone excepted.

Nor is this all. Whatever else our index may do or may not do, it certainly does not overstate the actual rate of increase. It does not take account of the commodity, Voluntary Leisure. New commodities escape or are inadequately represented by an index which must rest largely on basic commodities and intermediate products. For the same reason improvements in quality almost completely fail to assert themselves although they constitute, in many lines, the core of the progress achieved—there is no way of expressing adequately the difference between a motorcar of 1940 and a motorcar of 1900 or the extent to which the price of motorcars per unit of utility has fallen. It would be more nearly possible to estimate the rate at which given quantities of raw materials or semi-finished products are made to go further than they used to—a steel ingot or a ton of coal, though they may be unchanged in physical quality, represent a multiple of their economic efficiency sixty years ago. But little has been done along this line. I have no idea about what would happen to our index if there were a method for correcting it for these and similar factors. It is certain, however, that its percentage rate of change would be increased and that we have here a reserve that should make the estimate adopted proof against the effects of any conceivable downward revision. Moreover, even if we had the means of measuring the change in the technological efficiency of industrial products, this measure would still fail to convey an adequate idea of what it means for the dignity or intensity or pleasantness of human life—for all that the economists of an earlier generation subsumed under the heading of Satisfaction of Wants. And this, after all, is for us the relevant consideration, the true "output" of capitalist production, the reason

[8] See Stamp, *op. cit.* The same phenomenon can be observed in all countries for which there is sufficient statistical information, if we clear the latter of the disturbing effect of the cycles of various span that are covered by the available material. The measure of income distribution (or of inequality of incomes) devised by Vilfredo Pareto is open to objection. But the fact itself is independent of its shortcomings.

why we are interested in the index of production and the pounds and gallons that enter into it and would hardly be worth while in themselves.

But let us keep to our 2 per cent. There is one more point that is important for a correct appraisal of that figure. I have stated above that, broadly speaking, relative shares in national income have remained substantially constant over the last hundred years. This, however, is true only if we measure them in money. Measured in real terms, relative shares have substantially changed in favor of the lower income groups. This follows from the fact that the capitalist engine is first and last an engine of mass production which unavoidably means also production for the masses, whereas, climbing upward in the scale of individual incomes, we find that an increasing proportion is being spent on personal services and on handmade commodities, the prices of which are largely a function of wage rates.

Verification is easy. There are no doubt some things available to the modern workman that Louis XIV himself would have been delighted to have yet was unable to have—modern dentistry for instance. On the whole, however, a budget on that level had little that really mattered to gain from capitalist achievement. Even speed of traveling may be assumed to have been a minor consideration for so very dignified a gentleman. Electric lighting is no great boon to anyone who has money enough to buy a sufficient number of candles and to pay servants to attend to them. It is the cheap cloth, the cheap cotton and rayon fabric, boots, motorcars and so on that are the typical achievements of capitalist production, and not as a rule improvements that would mean much to the rich man. Queen Elizabeth owned silk stockings. The capitalist achievement does not typically consist in providing more silk stockings for queens but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort.

The same fact stands out still better if we glance at those long waves in economic activity, analysis of which reveals the nature and mechanism of the capitalist process better than anything else. Each of them consists of an "industrial revolution" and the absorption of its effects. For instance, we are able to observe statistically and historically—the phenomenon is so clear that even our scanty information suffices to establish it—the rise of such a long wave toward the end of the 1780's, its culmination around 1800, its downward sweep and then a sort of recovery ending at the beginning of the 1840's. This was the Industrial Revolution dear to the heart of textbook writers. Upon its heels, however, came another such revolution producing another long wave that rose in the forties, culminated just before 1857 and ebbed away to 1897, to be followed in turn by the one that reached its peak about 1911 and is now in the act of ebbing away.[9]

These revolutions periodically reshape the existing structure of industry by introducing new methods of production—the mechanized factory, the electrified factory, chemical synthesis and the like; new commodities, such as railroad service, motorcars, electrical appliances; new forms of organization—the merger movement; new sources of supply—La Plata wool, American cotton, Katanga copper; new trade routes and markets to sell in and so on. This process of industrial change provides the ground swell that gives the general tone to business: while these things are being initiated we have brisk expenditure and predominating "prosperity"—interrupted, no doubt, by the negative phases of the shorter cycles that are superimposed on that ground swell—and while those things are being completed and their results pour forth we have elimination of antiquated elements of the industrial structure and predominating "depression." Thus there are prolonged periods of rising and of falling prices, interest rates, employment and so on, which phenomena constitute parts of the mechanism of this process of recurrent rejuvenation of the productive apparatus.

Now these results each time consist in an avalanche of consumers' goods that permanently deepens and widens the stream of real income although in the first instance they spell disturbance, losses and unemployment. And if we look at those avalanches of consumers' goods we again find that each of them consists in articles of mass consumption and increases the purchasing power of the wage dollar more than that of any other dollar—in other words, that the capitalist process, not by coincidence but by virtue of its mechanism, progressively raises the standard of life of the masses. It does so through a sequence of vicissitudes, the severity of which is proportional to the speed of the advance. But it does so effectively. One problem after another of the supply of commodities to the masses has been successfully solved[10] by being brought within the reach of the methods of capitalist production. The most important one of those that remain, housing, is approaching solution by means of the pre-fabricated house.

And still this is not all. Appraisal of an economic order would be incomplete—and incidentally un-Marxian—if it stopped at the output which the corresponding economic conveyor hands to the various groups of society and left out of account all those things that the conveyor does not serve directly but for which it provides the means

[9] These are the "long waves" which, in business cycle literature, are primarily associated with the name of N. D. Kondratieff.

[10] This of course also applies to agricultural commodities, the cheap mass production of which was entirely the work of large-scale capitalist enterprise (railroads, shipping, agricultural machinery, fertilizers).

as well as the political volition, and all those cultural achievements that are induced by the mentality it generates. Deferring consideration of the latter (Chapter XI), we shall now turn to some aspects of the former.

The technique and atmosphere of the struggle for social legislation obscures the otherwise obvious facts that, on the one hand, part of this legislation presupposes previous capitalist success (in other words, wealth which had previously to be created by capitalist enterprise) and that, on the other hand, much of what social legislation develops and generalizes had been previously initiated by the action of the capitalist stratum itself. Both facts must of course be added to the sum total of capitalist performance. Now if the system had another run such as it had in the sixty years preceding 1928 and really reached the $1300 *per head of population*, it is easy to see that all the desiderata that have so far been espoused by any social reformers—practically without exception, including even the greater part of the cranks—either would be fulfilled automatically or could be fulfilled *without significant interference with the capitalist process*. Ample provision for the unemployed in particular, would then be not only a tolerable but a light burden. Irresponsibility in creating unemployment and in financing the support of the unemployed might of course at any time create insoluble problems. But managed with ordinary prudence, an *average* annual expenditure of 16 billions on an *average* number of 16 million unemployed including dependents (10 per cent of the population) would not in itself be a serious matter with an available national income of the order of magnitude of 200 billion dollars (purchasing power of 1928).

May I call the reader's attention to the reason why unemployment which everyone agrees must be one of the most important issues in any discussion of capitalism—with some critics so much so that they base their indictment exclusively on this element of the case—will play a comparatively small role in my argument? I do not think that unemployment is among those evils which, like poverty, capitalist evolution could ever eliminate of itself. I also do not think that there is any tendency for the unemployment percentage to increase in the long run. The only series covering a respectable time interval—roughly the sixty years preceding the First World War—gives the English trade-union percentage of unemployed members. It is a typically cyclical series and displays no trend (or a horizontal one).[11] Since this is theoretically understandable—there is no theoretical reason to call the evidence in question—those two propositions seem established for

[11] That series has often been charted and analyzed. See for instance, A. C. Pigou, *Industrial Fluctuations* or my *Business Cycles*. For every country there seems to be an irreducible minimum and, superimposed on that, a cyclical movement, the strongest component of which has a period of about nine to ten years.

the prewar time to 1913 inclusive. In the postwar time and in most countries unemployment was mostly at an abnormally high level even before 1930. But this and still more the unemployment during the thirties can be accounted for on grounds that have nothing to do with a long-run tendency of unemployment percentages to increase *from causes inherent in the capitalist mechanism itself.* I have mentioned above those industrial revolutions which are so characteristic of the capitalist process. Supernormal unemployment is one of the features of the periods of adaptation that follow upon the "prosperity phase" of each of them. We observe it in the 1820's and 1870's, and the period after 1920 is simply another of those periods. So far the phenomenon is essentially temporary in the sense that nothing can be inferred about it for the future. But there were a number of other factors which tended to intensify it—war effects, dislocations of foreign trade, wage policies, certain institutional changes that swelled the statistical figure, in England and Germany fiscal policies (also important in the United States since 1935) and so on. Some of these are no doubt symptoms of an "atmosphere" in which capitalism will work with decreasing efficiency. That however is another matter which will engage our attention later on.

But whether lasting or temporary, getting worse or not, unemployment undoubtedly is and always has been a scourge. In the next part of this book we shall have to list its possible elimination among the claims of the socialist order to superiority. Nevertheless, I hold that the real tragedy is not unemployment *per se,* but unemployment plus the impossibility of providing adequately for the unemployed *without impairing the conditions of further economic development:* for obviously the suffering and degradation—the destruction of human values—which we associate with unemployment, though not the waste of productive resources, would be largely eliminated and unemployment would lose practically all its terror if the private life of the unemployed were not seriously affected by their unemployment. The indictment stands that in the past—say, roughly, to the end of the nineteenth century—the capitalist order was not only unwilling but also quite incapable of guaranteeing this. But since it will be able to do so if it keeps up its past performance for another half century this indictment would in that case enter the limbo filled by the sorry specters of child labor and sixteen-hour working days and five persons living in one room which it is quite proper to emphasize when we are talking about the past social costs of capitalist achievement but which are not necessarily relevant to the balance of alternatives for the future. Our own time is somewhere between the disabilities of earlier stages in capitalist evolution and the abilities of the system in full maturity. In this country at least, the better part of the task could even now be accomplished without undue strain on the system. The

difficulties do not seem to consist so much in the lack of a surplus sufficient to blot out the darkest hues in the picture: they consist, on the one hand, in the fact that the unemployment figure has been increased by anti-capitalist policies beyond what it need have been in the thirties and, on the other hand, in the fact that public opinion as soon as it becomes at all alive to the duty in question, immediately insists on economically irrational methods of financing relief and on lax and wasteful methods of administering it.

Much the same argument applies to the future—and to a great extent the present—possibilities held out by capitalist evolution for the care of the aged and sick, for education and hygiene and so on. Also, an increasing number of commodities might reasonably be expected, from the standpoint of the individual household, to pass out of the class of economic goods and to be available practically up to the satiety point. This could be brought about either by arrangements between public agencies and producing concerns or by nationalization or municipalization, gradual progress with which would of course be a feature of the future development even of an otherwise unfettered capitalism.

CHAPTER VI

PLAUSIBLE CAPITALISM

THE argument of the preceding chapter seems to be exposed to a reply that is as damaging as it is obvious. The average rate of increase in total available production that obtained during the sixty years preceding 1928 has been projected into the future. So far as this was merely a device in order to illustrate the significance of past development, there was nothing in this procedure that could have shocked the statistical conscience. But as soon as I implied that the following fifty years might actually display a similar average rate of increase, I apparently did commit a statistical crime; it is, of course, clear that a historical record of production over any given period does not in itself justify any extrapolation at all,[1] let alone an extrapolation over half a century. It is therefore necessary to emphasize again that my extrapolation is not intended to forecast the actual behavior of output in the future. Beyond illustrating the meaning of past performance, it is merely intended to give us a quantitative idea of what the capitalist engine might conceivably accomplish if, for another half century, it repeated its past performance—which is a very different matter. The question whether it can be expected to do so will be answered quite independently of the extrapolation itself. For this purpose we have now to embark upon a long and difficult investigation.

Before we can discuss the chance of capitalism repeating its past performance we must evidently try to find out in what sense the observed rate of increase in output really measures that past performance. No doubt, the period that furnished our data was one of comparatively unfettered capitalism. But this fact does not in itself provide a sufficient link between the performance and the capitalist engine. In order to believe that this was more than coincidence we must satisfy ourselves first, that there is an understandable relation between the capitalist order and the observed rate of increase in output; second, that, given such a relation, the rate of increase was actually due to it and not to

[1] This proposition holds, on general principles, for any *historical* time series, since the very concept of historical sequence implies the occurrence of irreversible changes in the economic structure which must be expected to affect the law of any given economic quantity. Theoretical justification and, as a rule, statistical treatment are therefore necessary for even the most modest extrapolations. It may however be urged that our case is somewhat favored by the fact that within the comprehensive compound represented by the output series, idiosyncrasies of individual items will to some extent cancel each other.

particularly favorable conditions which had nothing to do with capitalism.

These two problems must be solved before the problem of a "repetition of performance" can arise at all. The third point then reduces to the question whether there is any reason why the capitalist engine should, during the next forty years, fail to go on working as it did in the past.

We shall deal with these three points in turn.

Our first problem may be reformulated as follows. On the one hand, we have a considerable body of statistical data descriptive of a rate of "progress" that has been admired even by very critical minds. On the other hand, we have a body of facts about the structure of the economic system of that period and about the way it functioned; from these facts, analysis has distilled what is technically called a "model" of capitalist reality, i.e., a generalized picture of its essential features. We wish to know whether that type of economy was favorable, irrelevant, or unfavorable to the performance we observe and, if favorable, whether those features may be reasonably held to yield adequate explanation of this performance. Waiving technicalities as much as possible, we shall approach the question in a common-sense spirit.

1. Unlike the class of feudal lords, the commercial and industrial bourgeoisie rose by business success. Bourgeois society has been cast in a purely economic mold: its foundations, beams and beacons are all made of economic material. The building faces toward the economic side of life. Prizes and penalties are measured in pecuniary terms. Going up and going down means making and losing money. This, of course, nobody can deny. But I wish to add that, within its own frame, that social arrangement is, or at all events was, singularly effective. In part it appeals to, and in part it creates, a schema of motives that is unsurpassed in simplicity and force. The promises of wealth and the threats of destitution that it holds out, it redeems with ruthless promptitude. Wherever the bourgeois way of life asserts itself sufficiently to dim the beacons of other social worlds, these promises are strong enough to attract the large majority of supernormal brains and to identify success with business success. They are not proffered at random; yet there is a sufficiently enticing admixture of chance: the game is not like roulette, it is more like poker. They are addressed to ability, energy and supernormal capacity for work; but if there were a way of measuring either that ability in general or the personal achievement that goes into any particular success, the premiums actually paid out would probably not be found proportional to either. Spectacular prizes much greater than would have been necessary to call forth the particular effort are thrown to a small minority of winners, thus propelling much more efficaciously than a

more equal and more "just" distribution would, the activity of that large majority of businessmen who receive in return very modest compensation or nothing or less than nothing, and yet do their utmost because they have the big prizes before their eyes and overrate their chances of doing equally well. Similarly, the threats are addressed to incompetence. But though the incompetent men and the obsolete methods are in fact eliminated, sometimes very promptly, sometimes with a lag, failure also threatens or actually overtakes many an able man, thus whipping up *everyone*, again much more efficaciously than a more equal and more "just" system of penalties would. Finally, both business success and business failure are ideally precise. Neither can be talked away.

One aspect of this should be particularly noticed, for future reference as well as because of its importance for the argument in hand. In the way indicated and also in other ways which will be discussed later on, the capitalist arrangement, as embodied in the institution of private enterprise, effectively chains the bourgeois stratum to its tasks. But it does more than that. The same apparatus which conditions for performance the individuals and families that at any given time form the bourgeois class, *ipso facto* also selects the individuals and families that are to rise into that class or to drop out of it. This combination of the conditioning and the selective function is not a matter of course. On the contrary, most methods of social selection, unlike the "methods" of biological selection, do not guarantee performance of the selected individual; and their failure to do so constitutes one of the crucial problems of socialist organization that will come up for discussion at another stage of our inquiry. For the time being, it should merely be observed how well the capitalist system solves that problem: in most cases the man who rises first *into* the business class and then *within* it is also an able businessman and he is likely to rise exactly as far as his ability goes—simply because in that schema rising to a position and doing well in it generally is or was one and the same thing. This fact, so often obscured by the auto-therapeutic effort of the unsuccessful to deny it, is much more important for an appraisal of capitalist society and its civilization than anything that can be gleaned from the pure theory of the capitalist machine.

2. But is not all that we might be tempted to infer from "maximum performance of an optimally selected group" invalidated by the further fact that that performance is not geared to social service—production, so we might say, for consumption—but to money-making, that it aims at maximizing profits instead of welfare? Outside of the bourgeois stratum, this has of course always been the popular opinion. Economists have sometimes fought and sometimes espoused it. In doing so they have contributed something that was much more valuable than were the final judgments themselves at which they arrived

individually and which in most cases reflect little more than their social location, interests and sympathies or antipathies. They slowly increased our factual knowledge and analytic powers so that the answers to many questions we are able to give today are no doubt much more correct although less simple and sweeping than were those of our predecessors.

To go no further back, the so-called classical economists[2] were practically of one mind. Most of them disliked many things about the social institutions of their epoch and about the way those institutions worked. They fought the landed interest and approved of social reforms—factory legislation in particular—that were not all on the lines of *laissez faire*. But they were quite convinced that within the institutional framework of capitalism, the manufacturer's and the trader's self-interest made for maximum performance in the interest of all. Confronted with the problem we are discussing, they would have had little hesitation in attributing the observed rate of increase in total output to relatively unfettered enterprise and the profit motive—perhaps they would have mentioned "beneficial legislation" as a condition but by this they would have meant the removal of fetters, especially the removal or reduction of protective duties during the nineteenth century.

It is exceedingly difficult, at this hour of the day, to do justice to these views. They were of course the typical views of the English bourgeois class, and bourgeois blinkers are in evidence on almost every page the classical authors wrote. No less in evidence are blinkers of another kind: the classics reasoned in terms of a particular historical situation which they uncritically idealized and from which they uncritically generalized. Most of them, moreover, seem to have argued exclusively in terms of the English interests and problems of their time. This is the reason why, in other lands and at other times, people disliked their economics, frequently to the point of not even caring to understand it. But it will not do to dismiss their teaching on these grounds. A prejudiced man may yet be speaking the truth. Propositions developed from special cases may yet be generally valid. And the enemies and successors of the classics had and have only different but not fewer blinkers and preconceptions; they envisaged and envisage different but not less special cases.

From the standpoint of the economic analyst, the chief merit of the classics consists in their dispelling, along with many other gross errors, the naïve idea that economic activity in capitalist society, because it

[2] The term Classical Economists will in this book be used to designate the leading English economists whose works appeared between 1776 and 1848. Adam Smith, Ricardo, Malthus, Senior and John Stuart Mill are the outstanding names. It is important to keep this in mind because a much broader use of the term has come into fashion of late.

turns on the profit motive, must by virtue of that fact alone necessarily run counter to the interests of consumers; or, to put it differently, that moneymaking necessarily deflects producing from its social goal; or, finally, that private profits, both in themselves and through the distortion of the economic process they induce, are always a net loss to all excepting those who receive them and would therefore constitute a net gain to be reaped by socialization. If we look at the logic of these and similar propositions which no trained economist ever thought of defending, the classical refutation may well seem trivial. But as soon as we look at all the theories and slogans which, consciously or subconsciously, imply them and which are once more served up today, we shall feel more respect for that achievement. Let me add at once that the classical writers also clearly perceived, though they may have exaggerated, the role of saving and accumulation and that they linked saving to the rate of "progress" they observed in a manner that was fundamentally, if only approximately, correct. Above all, there was practical wisdom about their doctrine, a responsible long-run view and a manly tone that contrast favorably with modern hysterics.

But between realizing that hunting for a maximum of profit and striving for maximum productive performance are not necessarily incompatible, to proving that the former will necessarily—or in the immense majority of cases—imply the latter, there is a gulf much wider than the classics thought. And they never succeeded in bridging it. The modern student of their doctrines never ceases to wonder how it was possible for them to be satisfied with their arguments or to mistake these arguments for proofs; in the light of later analysis their *theory* was seen to be a house of cards whatever measure of truth there may have been in their *vision*.[3]

3. This later analysis we will take in two strides—as much of it, that is, as we need in order to clarify our problem. Historically, the first will carry us into the first decade of this century, the second will cover some of the postwar developments of scientific economics. Frankly I do not know how much good this will do the non-professional reader; like every other branch of our knowledge, economics, as its analytic engine improves, moves fatally away from that happy stage in which all problems, methods and results could be made accessible to every educated person without special training. I will, however, do my best.

The first stride may be associated with two great names revered to

[3] The reader will recall my emphasis on the distinction between one's theory and one's vision in the case of Marx. It is however always important to remember that the ability to see things in their correct perspective may be, and often is, divorced from the ability to reason correctly and vice versa. That is why a man may be a very good theorist and yet talk absolute nonsense whenever confronted with the task of diagnosing a concrete historical pattern as a whole.

this day by numberless disciples—so far at least as the latter do not think it bad form to express reverence for anything or anybody, which many of them obviously do—Alfred Marshall and Knut Wicksell.[4] Their theoretical structure has little in common with that of the classics—though Marshall did his best to hide the fact—but it conserves the classic proposition that in the case of perfect competition the profit interest of the producer tends to maximize production. It even supplied almost satisfactory proof. Only, in the process of being more correctly stated and proved, the proposition lost much of its content—it does emerge from the operation, to be sure, but it emerges emaciated, barely alive.[5] Still it can be shown, within the general assumptions of the Marshall-Wicksell analysis, that firms which cannot by their own individual action exert any influence upon the price of their products or of the factors of production they employ—so that there would be no point in their weeping over the fact that any increase in production tends to decrease the former and to increase the latter—will expand their output until they reach the point at which the additional cost that must be incurred in order to produce another small increment of product (marginal cost) just equals the price they

[4] Marshall's *Principles* (first edition 1890) and Wicksell's *Lectures* (first Swedish edition 1901, English translation 1934) are entitled to the prominence I am here giving to them, because of the influence they exerted on many minds in their formative stages and because they dealt with theory in a thoroughly practical spirit. On purely scientific grounds, precedence should be given to the work of Léon Walras. In America, the names to mention are J. B. Clark, Irving Fisher and F. W. Taussig.

[5] Anticipating later argument (see below, ch. viii, § 6) I shall in this note briefly clarify the above passage. Analysis of the mechanism of the profit economy led not only to the discovery of exceptions to the principle that competitive industry tends to maximize output, but also to the discovery that proof of the principle itself requires assumptions which reduce it to little more than a truism. Its practical value is however particularly impaired by the two following considerations:

1. The principle, as far as it can be proved at all, applies to a state of static equilibrium. Capitalist reality is first and last a process of change. In appraising the performance of competitive enterprise, the question whether it would or would not tend to maximize production in a perfectly equilibrated stationary condition of the economic process is hence almost, though not quite, irrelevant.

2. The principle, as stated by Wicksell, is what was left of a more ambitious proposition that, though in a rarefied form, can still be found in Marshall—the theorem that competitive industry tends to produce a state of maximum satisfaction of wants. But this theorem, even if we waive the serious objections to speaking of non-observable psychic magnitudes, is readily seen to boil down to the triviality that, whatever the data and in particular the institutional arrangements of a society may be, human action, as far as it is rational, will always try to make the best of any given situation. In fact it boils down to a definition of rational action and can hence be paralleled by analogous theorems for, say, a socialist society. But so can the principle of maximum production. Neither formulates any specific virtue of private competitive enterprise. This does not mean that such virtues do not exist. It does mean however that they are not simply inherent in the *logic* of competition.

can get for that increment, i.e., that they will produce as much as they can without running into loss. And this can be shown to be as much as it is in general "socially desirable" to produce. In more technical language, in that case prices are, from the standpoint of the individual firm, not variables but parameters; and where this is so, there exists a state of equilibrium in which all outputs are at their maximum and all factors fully employed. This case is usually referred to as perfect competition. Remembering what has been said about the selective process which operates on all firms and their managers, we might in fact conceive a very optimistic idea of the results to be expected from a highly selected group of people forced, within that pattern, by their profit motive to strain every nerve in order to maximize output and to minimize costs. In particular, it might seem at first sight that a system conforming to this pattern would display remarkable absence of some of the major sources of social waste. As a little reflection should show, this is really but another way of stating the content of the preceding sentence.

4. Let us take the second stride. The Marshall-Wicksell analysis of course did not overlook the many cases that fail to conform to that model. Nor, for that matter, had the classics overlooked them. They recognized cases of "monopoly," and Adam Smith himself carefully noticed the prevalence of devices to restrict competition[6] and all the differences in flexibility of prices resulting therefrom. But they looked upon those cases as exceptions and, moreover, as exceptions that could and would be done away with in time. Something of that sort is true also of Marshall. Although he developed the Cournot theory of monopoly[7] and although he anticipated later analysis by calling attention to the fact that most firms have special markets of their own in which they set prices instead of merely accepting them,[8] he as well as Wicksell framed his general conclusions on the pattern of perfect competition so as to suggest, much as the classics did, that perfect competition was the rule. Neither Marshall and Wicksell nor the classics saw that perfect competition is the exception and that even if it were the rule there would be much less reason for congratulation than one might think.

If we look more closely at the conditions—not all of them explicitly stated or even clearly seen by Marshall and Wicksell—that must be fulfilled in order to produce perfect competition, we realize immediately that outside of agricultural mass production there cannot be many instances of it. A farmer supplies his cotton or wheat in fact under those conditions: from his standpoint the ruling prices of cotton or wheat are data, though very variable ones, and not being able to influence them by his individual action he simply adapts his output; since all farmers do the same, prices and quantities will in the end be adjusted as the theory of perfect competition requires. But this is not so even with many agricultural products—with ducks, sausages, vegetables and many dairy products for instance. And as regards practically all the finished products and services of industry and trade, it is clear that every grocer, every filling station, every manufacturer of gloves or shaving cream or handsaws has a small and precarious market of his own which he tries—must try—to build up and to keep by price strategy, quality strategy—"product differentiation"—and advertising. Thus we get a completely different pattern which there seems to be no reason to expect to yield the results of perfect competition and which fits much better into the monopolistic schema. In these cases we speak of Monopolistic Competition. Their theory has been one of the major contributions to postwar economics.[9]

There remains a wide field of substantially homogeneous products—mainly industrial raw materials and semi-finished products such as steel ingots, cement, cotton gray goods and the like—in which the conditions for the emergence of monopolistic competition do not seem to prevail. This is so. But in general, similar results follow for that field inasmuch as the greater part of it is covered by largest-scale firms which, either individually or in concert, are able to manipulate prices even without differentiating products—the case of Oligopoly. Again the monopoly schema, suitably adapted, seems to fit this type of behavior much better than does the schema of perfect competition.

As soon as the prevalence of monopolistic competition or of oligopoly or of combinations of the two is recognized, many of the propositions which the Marshall-Wicksell generation of economists used to teach with the utmost confidence become either inapplicable or much more difficult to prove. This holds true, in the first place, of the propositions turning on the fundamental concept of equilibrium, i.e., a determinate state of the economic organism, toward which any given state of it is always gravitating and which displays certain simple properties. In the general case of oligopoly there is in fact no determinate equilibrium at all and the possibility presents itself that there may be an endless sequence of moves and countermoves, an indefinite state of warfare between firms. It is true that there are many special cases in which a state of equilibrium theoretically exists. In the second place, even in these cases not only is it much harder to attain than

[6] In a manner strikingly suggestive of present-day attitudes he even emphasized the discrepancy between the interests of every trade and those of the public and talked about conspiracies against the latter which, so he thought, might originate at any businessmen's dinner party.

[7] Augustin Cournot, 1938.

[8] This is why the later theory of imperfect competition may fairly be traced to him. Though he did not elaborate it, he saw the phenomenon more correctly than most of those who did. In particular he did not exaggerate its importance.

[9] See, in particular, E. S. Chamberlin, *Theory of Monopolistic Competition*, and Joan Robinson, *The Economics of Imperfect Competition*.

the equilibrium in perfect competition, and still harder to preserve, but the "beneficial" competition of the classic type seems likely to be replaced by "predatory" or "cutthroat" competition or simply by struggles for control in the financial sphere. These things are so many sources of social waste, and there are many others such as the costs of advertising campaigns, the suppression of new methods of production (buying up of patents in order not to use them) and so on. And most important of all: under the conditions envisaged, equilibrium, even if eventually attained by an extremely costly method, no longer guarantees either full employment or maximum output in the sense of the theory of perfect competition. It *may* exist without full employment; it is *bound* to exist, so it seems, at a level of output below that maximum mark, because profit-conserving strategy, impossible in conditions of perfect competition, now not only becomes possible but imposes itself.

Well, does not this bear out what the man in the street (unless a businessman himself) always thought on the subject of private business? Has not modern analysis completely refuted the classical doctrine and justified the popular view? Is it not quite true after all, that there is little parallelism between producing for profit and producing for the consumer and that private enterprise is little more than a device to curtail production in order to extort profits which then are correctly described as tolls and ransoms?

CHAPTER VII

THE PROCESS OF CREATIVE DESTRUCTION

THE theories of monopolistic and oligopolistic competition and their popular variants may in two ways be made to serve the view that capitalist reality is unfavorable to maximum performance in production. One may hold that it always has been so and that all along output has been expanding in spite of the secular sabotage perpetrated by the managing bourgeoisie. Advocates of this proposition would have to produce evidence to the effect that the observed rate of increase can be accounted for by a sequence of favorable circumstances unconnected with the mechanism of private enterprise and strong enough to overcome the latter's resistance. This is precisely the question which we shall discuss in Chapter IX. However, those who espouse this variant at least avoid the trouble about historical fact that the advocates of the alternative proposition have to face. This avers that capitalist reality once tended to favor maximum productive performance, or at all events productive performance so considerable as to constitute a major element in any serious appraisal of the system; but that the later spread of monopolist structures, killing competition, has by now reversed that tendency.

First, this involves the creation of an entirely imaginary golden age of perfect competition that at some time somehow metamorphosed itself into the monopolistic age, whereas it is quite clear that perfect competition has at no time been more of a reality than it is at present. Secondly, it is necessary to point out that the rate of increase in output did not decrease from the nineties from which, I suppose, the prevalence of the largest-size concerns, at least in manufacturing industry, would have to be dated; that there is nothing in the behavior of the time series of total output to suggest a "break in trend"; and, most important of all, that the modern standard of life of the masses evolved during the period of relatively unfettered "big business." If we list the items that enter the modern workman's budget and from 1899 on observe the course of their prices not in terms of money but in terms of the hours of labor that will buy them—i.e., each year's money prices divided by each year's hourly wage rates—we cannot fail to be struck by the rate of the advance which, considering the spectacular improvement in qualities, seems to have been greater and not smaller than it ever was before. If we economists were given less to wishful thinking and more to the observation of facts, doubts would immediately arise as to the realistic virtues of a theory that would have led us to expect a very different result. Nor is this all. As soon as we go into details and inquire into the individual items in which progress was most conspicuous, the trail leads not to the doors of those firms that work under conditions of comparatively free competition but precisely to the doors of the large concerns—which, as in the case of agricultural machinery, also account for much of the progress in the competitive sector—and a shocking suspicion dawns upon us that big business may have had more to do with creating that standard of life than with keeping it down.

The conclusions alluded to at the end of the preceding chapter are in fact almost completely false. Yet they follow from observations and theorems that are almost completely[1] true. Both economists and popular writers have once more run away with some fragments of reality they happened to grasp. These fragments themselves were mostly seen correctly. Their formal properties were mostly developed correctly. But no conclusions about capitalist reality as a whole follow from such fragmentary analyses. If we draw them nevertheless, we can be right only by accident. That has been done. And the lucky accident did not happen.

The essential point to grasp is that in dealing with capitalism we are dealing with an evolutionary process. It may seem strange that anyone can fail to see so obvious a fact which moreover was long ago emphasized by Karl Marx. Yet that fragmentary analysis which yields the bulk of our propositions about the functioning of modern capitalism persistently neglects it. Let us restate the point and see how it bears upon our problem.

Capitalism, then, is by nature a form or method of economic change and not only never is but never can be stationary. And this evolutionary character of the capitalist process is not merely due to the fact that economic life goes on in a social and natural environment which changes and by its change alters the data of economic action; this fact is important and these changes (wars, revolutions and so on) often condition industrial change, but they are not its prime movers. Nor is this evolutionary character due to a quasi-automatic increase in population and capital or to the vagaries of monetary systems of

[1] As a matter of fact, those observations and theorems are not completely satisfactory. The usual expositions of the doctrine of imperfect competition fail in particular to give due attention to the many and important cases in which, even as a matter of static theory, imperfect competition approximates the results of perfect competition. There are other cases in which it does not do this, but offers compensations which, while not entering any output index, yet contribute to what the output index is in the last resort intended to measure—the cases in which a firm defends its market by establishing a name for quality and service for instance. However, in order to simplify matters, we will not take issue with that doctrine on its own ground.

which exactly the same thing holds true. The fundamental impulse that sets and keeps the capitalist engine in motion comes from the new consumers' goods, the new methods of production or transportation, the new markets, the new forms of industrial organization that capitalist enterprise creates.

As we have seen in the preceding chapter, the contents of the laborer's budget, say from 1760 to 1940, did not simply grow on unchanging lines but they underwent a process of qualitative change. Similarly, the history of the productive apparatus of a typical farm, from the beginnings of the rationalization of crop rotation, plowing and fattening to the mechanized thing of today—linking up with elevators and railroads—is a history of revolutions. So is the history of the productive apparatus of the iron and steel industry from the charcoal furnace to our own type of furnace, or the history of the apparatus of power production from the overshot water wheel to the modern power plant, or the history of transportation from the mailcoach to the airplane. The opening up of new markets, foreign or domestic, and the organizational development from the craft shop and factory to such concerns as U. S. Steel illustrate the same process of industrial mutation—if I may use that biological term—that incessantly revolutionizes[2] the economic structure *from within*, incessantly destroying the old one, incessantly creating a new one. This process of Creative Destruction is the essential fact about capitalism. It is what capitalism consists in and what every capitalist concern has got to live in. This fact bears upon our problem in two ways.

First, since we are dealing with a process whose every element takes considerable time in revealing its true features and ultimate effects, there is no point in appraising the performance of that process *ex visu* of a given point of time; we must judge its performance over time, as it unfolds through decades or centuries. A system—any system, economic or other—that at *every* given point of time fully utilizes its possibilities to the best advantage may yet in the long run be inferior to a system that does so at *no* given point of time, because the latter's failure to do so may be a condition for the level or speed of long-run performance.

Second, since we are dealing with an organic process, analysis of what happens in any particular part of it—say, in an individual concern or industry—may indeed clarify details of mechanism but is inconclusive beyond that. Every piece of business strategy acquires its true significance only against the background of that process and

[2] Those revolutions are not strictly incessant; they occur in discrete rushes which are separated from each other by spans of comparative quiet. The process as a whole works incessantly however, in the sense that there always is either revolution or absorption of the results of revolution, both together forming what are known as business cycles.

within the situation created by it. It must be seen in its role in the perennial gale of creative destruction; it cannot be understood irrespective of it or, in fact, on the hypothesis that there is a perennial lull.

But economists who, *ex visu* of a point of time, look for example at the behavior of an oligopolist industry—an industry which consists of a few big firms—and observe the well-known moves and countermoves within it that seem to aim at nothing but high prices and restrictions of output are making precisely that hypothesis. They accept the data of the momentary situation as if there were no past or future to it and think that they have understood what there is to understand if they interpret the behavior of those firms by means of the principle of maximizing profits with reference to those data. The usual theorist's paper and the usual government commission's report practically never try to see that behavior, on the one hand, as a result of a piece of past history and, on the other hand, as an attempt to deal with a situation that is sure to change presently—as an attempt by those firms to keep on their feet, on ground that is slipping away from under them. In other words, the problem that is usually being visualized is how capitalism administers existing structures, whereas the relevant problem is how it creates and destroys them. As long as this is not recognized, the investigator does a meaningless job. As soon as it is recognized, his outlook on capitalist practice and its social results changes considerably.[8]

The first thing to go is the traditional conception of the *modus operandi* of competition. Economists are at long last emerging from the stage in which price competition was all they saw. As soon as quality competition and sales effort are admitted into the sacred precincts of theory, the price variable is ousted from its dominant position. However, it is still competition within a rigid pattern of invariant conditions, methods of production and forms of industrial organization in particular, that practically monopolizes attention. But in capitalist reality as distinguished from its textbook picture, it is not that kind of competition which counts but the competition from the new commodity, the new technology, the new source of supply, the new type of organization (the largest-scale unit of control for instance)—competition which commands a decisive cost or quality advantage and which strikes not at the margins of the profits and the outputs of the existing firms but at their foundations and their very lives. This kind of competition is as much more effective than the other as a bombardment is in comparison with forcing a door, and

[8] It should be understood that it is only our appraisal of economic performance and not our moral judgment that can be so changed. Owing to its autonomy, moral approval or disapproval is entirely independent of our appraisal of social (or any other) results, unless we happen to adopt a moral system such as utilitarianism which makes moral approval and disapproval turn on them *ex definitione*.

so much more important that it becomes a matter of comparative indifference whether competition in the ordinary sense functions more or less promptly; the powerful lever that in the long run expands output and brings down prices is in any case made of other stuff.

It is hardly necessary to point out that competition of the kind we now have in mind acts not only when in being but also when it is merely an ever-present threat. It disciplines before it attacks. The businessman feels himself to be in a competitive situation even if he is alone in his field or if, though not alone, he holds a position such that investigating government experts fail to see any effective competition between him and any other firms in the same or a neighboring field and in consequence conclude that his talk, under examination, about his competitive sorrows is all make-believe. In many cases, though not in all, this will in the long run enforce behavior very similar to the perfectly competitive pattern.

Many theorists take the opposite view which is best conveyed by an example. Let us assume that there is a certain number of retailers in a neighborhood who try to improve their relative position by service and "atmosphere" but avoid price competition and stick as to methods to the local tradition—a picture of stagnating routine. As others drift into the trade that quasi-equilibrium is indeed upset, but in a manner that does not benefit their customers. The economic space around each of the shops having been narrowed, their owners will no longer be able to make a living and they will try to mend the case by raising prices in tacit agreement. This will further reduce their sales and so, by successive pyramiding, a situation will evolve in which increasing potential supply will be attended by increasing instead of decreasing prices and by decreasing instead of increasing sales.

Such cases do occur, and it is right and proper to work them out. But as the practical instances usually given show, they are fringe-end cases to be found mainly in the sectors furthest removed from all that is most characteristic of capitalist activity.[4] Moreover, they are transient by nature. In the case of retail trade the competition that matters arises not from additional shops of the same type, but from the department store, the chain store, the mail-order house and the supermarket which are bound to destroy those pyramids sooner or later.[5]

[4] This is also shown by a theorem we frequently meet with in expositions of the theory of imperfect competition, viz., the theorem that, under conditions of imperfect competition, producing or trading businesses tend to be irrationally small. Since imperfect competition is at the same time held to be an outstanding characteristic of modern industry we are set to wondering what world these theorists live in, unless, as stated above, fringe-end cases are all they have in mind.

[5] The mere threat of their attack cannot, in the particular conditions, environmental and personal, of small-scale retail trade, have its usual disciplining influence, for the small man is too much hampered by his cost structure and, however

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Now a theoretical construction which neglects this essential element of the case neglects all that is most typically capitalist about it; even if correct in logic as well as in fact, it is like *Hamlet* without the Danish prince.

well he may manage within his inescapable limitations, he can never adapt himself to the methods of competitors who can afford to sell at the price at which he buys.

CHAPTER VIII

MONOPOLISTIC PRACTICES

What has been said so far is really sufficient to enable the reader to deal with the large majority of the practical cases he is likely to meet and to realize the inadequacy of most of those criticisms of the profit economy which, directly or indirectly, rely on the absence of perfect competition. Since, however, the bearing of our argument on some of those criticisms may not be obvious at a glance, it will be worth our while to elaborate a little in order to make a few points more explicit.

1. We have just seen that, both as a fact and as a threat, the impact of new things—new technologies for instance—on the existing structure of an industry considerably reduces the long-run scope and importance of practices that aim, through restricting output, at conserving established positions and at maximizing the profits accruing from them. We must now recognize the further fact that restrictive practices of this kind, as far as they are effective, acquire a new significance in the perennial gale of creative destruction, a significance which they would not have in a stationary state or in a state of slow and balanced growth. In either of these cases restrictive strategy would produce no result other than an increase in profits at the expense of buyers except that, in the case of balanced advance, it might still prove to be the easiest and most effective way of collecting the means by which to finance additional investment.[1] But in the process of creative destruction, restrictive practices may do much to steady the ship and to alleviate temporary difficulties. This is in fact a very familiar argument which always turns up in times of depression and, as everyone knows, has become very popular with governments and their economic advisers—witness the NRA. While it has been so much misused and so faultily acted upon that most economists heartily despise it, those

[1] Theorists are apt to look upon anyone who admits this possibility as guilty of gross error, and to prove immediately that financing by borrowing from banks or from private savers or, in the case of public enterprise, financing from the proceeds of an income tax is much more rational than is financing from surplus profits collected through a restrictive policy. For some patterns of behavior they are quite right. For others they are quite wrong. I believe that both capitalism and communism of the Russian type belong in the latter category. But the point is that theoretical considerations, especially theoretical considerations of the short-run kind, cannot solve, although they contribute to the solution of, the problem which we shall meet again in the next part.

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