

Was Keynes a Corporatist?
Keynes' s Radical Views on Industrial Policy and Macro Policy in the 1920s

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I. Introduction

Keynes' s main purpose in writing The Economic Consequences of the Peace (1919) was to issue a dire warning that if the provisions of the Treaty of Versailles were implemented, the world would face the prospect of economic stagnation, financial crisis, social and political unrest and, in some countries, possible revolution. But he also used the book to express his belief that Europe stood between two epochs of economic history. World War I accelerated the dissolution of the old order to be sure, and the Treaty threatened to make a peaceful and smooth transition to a new socioeconomic regime impossible, but Keynes believed that the old order was destined to crumble anyway.

Keynes argued that the conditions which made possible the high growth rate in Europe and North America between 1870 and World War I were inherently transitory. In the second sentence of the book he states that "very few of us realize with conviction the intensely unusual, unstable, complicated, unreliable, temporary nature of the economic organization by which Western Europe has lived for the last half century". Toward the book's end, he drew the following conclusion:

England is in a state of transition, and her economic problems are serious. We may be on the eve of great changes in her social and industrial structure (2, 253).¹

The most serious problems for England have been brought to a head by the war, but are in their origins more fundamental. The forces of the nineteenth century have run their course and are exhausted. The economic motives and ideals of that generation no longer satisfy us: we must find a new way and must suffer again the malaise, and finally the pangs, of a new industrial birth (2, 254).

In the mid 1920s, when Keynes's vision of this new order solidified, he proposed radical

new forms of state economic regulation at both the macro and microeconomic levels.

Unfortunately, his approach to both macro and microeconomic theory and policy has been widely misconceived. Recently, a small literature correctly reinterpreting Keynes's macro policy views has appeared.² Grounded primarily in his 1940s wartime writings, this literature reminds the reader that Keynes opposed such standard "Keynesian" tools as permanent deficit spending, and the use of tax and interest rates as counter-cyclical policy tools. Rather, he believed that we should rely on large-scale, long-term public investment as the cornerstone of aggregate demand management. However, as we show in the body of the paper, Keynes first announced his allegiance to the socialisation of investment³ not toward the end of his life, but in the mid 1920s.

Very little has been written, at least in recent decades, about Keynes's radical rethinking of microeconomic theory and policy in the 1920s. The traditional view that Keynes was uninterested in micro theory and was content to accept then-current orthodoxy about it is profoundly mistaken.³ The main purpose of this essay is to show just how badly off-base this conventional wisdom is, at least as applied to the 1920s. In that decade Keynes decisively rejected the traditional theory of perfect competition, applauded the ongoing trend toward increased reliance on public corporations, and argued that the government should not only accept the current movement toward cartels, holding companies, trade associations, pools and other forms of monopoly power, but should proactively assist and accelerate this trend in order to regulate and control it. When Keynes heralded the death of laissez-faire in the 1920s, it was not just macroeconomic policy he had in mind. He called with equal enthusiasm for the state to adopt powerful industrial policies to regulate enterprise and industry behavior. At least in this

period, **Keynes was unabashedly corporatist.**

The paper is organized as follows. Section II evaluates Keynes's more visionary mid 1920s essays in light of the main themes of this essay. Section III then discusses his critique of competitive markets and support for industrial policy in 1926-28. Section IV, a study of Keynes's work on the Liberal Party's 1928 book, Britain's Industrial Future, brings his macro and micro policies together. Finally, Section V discusses the relation of Keynes's views in the 1920s to his writings in the two decades which followed.

II. Visionary Essays: 1925-26

The publication of "Does Unemployment Need a Drastic Remedy?" in May 1924 in The Nation and Athenaeum, the Liberal Party journal, should be seen as the beginning of the "real" Keynesian revolution. It contained the initial statement and defense of the macro-policy position he fought for until his death in 1946 -- that the State should guide the national economy primarily through a permanent program of large-scale public investment. Though the theoretical defense of this policy would not be fully in place until the early 1930s, the broad outline of his policy perspective is clearly established in this 1924 article and in his subsequent debate with its critics.

Keynes's concrete policy proposal was for the Treasury to initiate and finance "expenditures up to (say) $\hat{100,000,000}$ a year" -- about 2.6 per cent of 1924 GDP -- "on the construction of capital works at home, enlisting in various ways the aid of private genius, temperament, and skill" (19, 222). He suggested that such a sum would be "enough to make good the wastage of nearly 500,000 men in unemployment" (19, 427), a decrease which would

have cut the unemployment rate from 10.3 to about 6 per cent. In summing up his position for his critics Keynes gives a clear reading on his general views on macro policy at this time.

In considering how to [raise the rate of capital accumulation], we are brought to my heresy -- if it is a heresy. I bring in the State; I abandon laissez-faire, -- not enthusiastically, not from contempt of that good old doctrine, but because, whether we like it or not, the conditions for its success have disappeared. ... There is no going back on this. The forces which press us may be blind, but they exist and are strong.

... the next developments of politico-economic evolution will emerge from new experiments directed towards determining the appropriate spheres of individual and government action. And to proceed to particulars, I suggest that the state encouragement of new capital undertakings, by employing the best technical advice to lay the foundations of great schemes, and by lending the credit and the guarantee of the Treasury to finance them more boldly than hitherto, is becoming an inevitable policy. (19, 228-29)

In other words, public capital accumulation to raise the trend rate of economic growth -- a new macroeconomic policy -- was a necessary (though not sufficient) condition for the solution of Britain's long-term unemployment problem.

The conventional view that Keynes mistakenly believed that British unemployment in the 1920s was caused by deficient aggregate demand is not correct. He agreed with the consensus opinion that unemployment was primarily structural in character, concentrated in Britain's key export industries.

If the figures be analysed we find a great concentration of unemployment in the shipbuilding and engineering industries (i.e., nearly four times the percentage elsewhere).

Outside these industries, unemployment amongst adult males does not now exceed much more than 4 per cent of the employable population. (19, 219)

There were two decidedly non-conventional aspects of Keynes' position, however. First, he believed that the standard policy to revive exports to prewar levels by attacking unions,

slashing wages, and driving down export prices was disastrously ill-conceived. The decline of Britain's export dominance was, in his view, permanent. Second, he argued that structural unemployment could not be vanquished unless the pace of national economic growth accelerated substantially. These structural or microeconomic problems could not be eliminated in the absence of a radical change in the approach to macroeconomics. Dramatic, complementary innovations in both micro and macro policy would be necessary. Britain

cannot cure these ills by the pressure of starvation, or by breaking the power for evil, and perhaps for good also, of the trade unions, or by reducing wages in the sheltered industries to the level of the unsheltered. From these thoughts the mind must be averted, for from such directions help will not come. Rather, we must seek to submerge the rocks in a rising sea, -- not forcing labour out of what is depressed, but attracting it into what is prosperous; not crushing the blind strength of organised labour, but relieving its fears, not abating wages where they are high, but raising them where they are low. (19, 221)

Keynes elaborated his radical vision of political economy and extended it to the micro level in a series of articles published in 1925 and 1926. Two of these -- "The End of Laissez-Faire" and "Am I A Liberal" -- are especially important.

In "The End of Laissez-Faire" (1926), Keynes presents a compelling micro-theoretical attack on unregulated competition as the central means of economic coordination.⁴ He attributes the rise of laissez-faire to developments in politics, philosophy, biology, economics, and in the performance of the British economy in the 18th and 19th centuries. One major influence was the intellectual dominance of Darwin's theory of evolution. Keynes argues that the theory of evolution, with its emphasis on sexual or reproductive competition as the driving force behind the natural selection of the "fittest", reinforced the belief that unregulated competition allocated economic assets to those who could use them most productively.

The economists were teaching that wealth, commerce, and machinery were the children of competition -- that free competition built London. But the Darwinians could go one

better than that -- free competition had built man. The human eye was [no longer] seen as the demonstration of [divine] design, miraculously contriving all things for the best; it was the supreme achievement of chance, operating under conditions of free competition and laissez-faire. (9, 276)

Keynes's attack had two components. The first argued that received economic theory considers only equilibrium states, paying no attention to the destructive properties of disequilibrium competitive processes. This argument is presented by way of analogy with a typical Darwinian story of how "ruthless" competition among giraffes for access to tree leaves leads to their optimal distribution from an evolutionary perspective. The second is a powerful critique of the theory of equilibrium states under perfect competition.

We consider the latter argument first. The proper method of analyzing the properties of a free-market system, Keynes tells us, has two-stages. The first is based on the simplest and most analytically tractable set of assumptions. In the second stage, realistic assumptions about key institutions and processes are substituted for the simplistic assumptions of the first stage. Only the more realistic second-stage model can be properly used to deduce guidelines for government policy. A fatal flaw in the argument of supporters of laissez-faire, then, is that their policy conclusions are based on an economic theory built on the "unreal assumptions" of stage one.

Keynes sums up this argument as follows:

The beauty and the simplicity of [orthodox] theory are so great that it is easy to forget that it follows not from the actual facts, but from an incomplete hypothesis introduced for the sake of simplicity. Apart from other objections [about disequilibrium processes] to be introduced later, the conclusion that individuals acting independently for their own advantage will produce the greatest aggregate of wealth, depends on a variety of unreal assumptions to the effect that the processes of production and consumption are in no way organic, that there exists a sufficient foreknowledge of conditions and requirements, and that there are adequate opportunities of obtaining this foreknowledge. For economists generally reserve for a later stage of their argument the complications which arise -- (1) when the efficient units of production are large relative to the units of consumption, (2) when overhead costs or joint costs are present, (3) when internal economies tend to the aggregation of production, (4) when the time required for adjustments is long, (5) when

ignorance prevails over knowledge, and (6) when monopolies and combination interfere with equality in bargaining -- they reserve, that is to say, for a later stage of their analysis the actual facts. (9, 284-85)

Realistic assumptions, Keynes insists, are a sine qua non of the scientific method in economics. Under assumptions that reflect the most relevant "actual facts" -- such as the organic structure of the economy, economies of scale, the existence of time, ignorance and fundamental uncertainty, and the impact of monopoly elements -- the conclusion that the equilibrium position achieved by unregulated competition is optimal can not be sustained. His analysis is consistent with the emphasis placed on the issue of organic versus atomistic economic structures in his earlier Treatise on Probability, while his concern with time, ignorance and "Keynesian" uncertainty prefigures his stress on these topics in The General Theory. Meanwhile, his focus on economies of scale, overhead costs, and monopolies and combinations reflects his current interest in industrial self-regulation and industrial policy as substitutes for coordination by atomistic competition.

We turn next to Keynes's charge that orthodox theory fails to theorize the disequilibrium properties of the perfectly or ruthlessly competitive system. Here he stresses the "parallelism between economic laissez-faire and Darwinism".

Just as Darwin invoked sexual love, acting through sexual selection, as an adjutant to natural selection by competition, to direct evolution along lines which should be desirable as well as effective, so the individualist invokes the love of money, acting through the pursuit of profit, as an adjutant to natural selection, to bring about the production on the greatest possible scale of what is most strongly desired as measured by exchange value. (9, 284)

The key parallel deals with the process through which wealth or "the instruments of production" are distributed among individuals. In Darwinian theory, if only we leave the giraffes to compete among themselves for access to leaves "the maximum quantity of leaves will

be cropped because the giraffes with the longest necks will, by dint of starving out the others, get nearest to the trees" (9, 283). Analogously, in the economic theory underlying laissez-faire:

the ideal distribution of productive resources can be brought about through individuals acting independently by the method of trial and error in such a way that those individuals who move in the right direction will destroy by competition those individuals who move in the wrong direction. This implies that there must be no mercy or protection for those who embark their capital or their labour in the wrong direction. It is a method of bringing the most successful profit-makers to the top by a ruthless struggle for survival, which selects the most efficient by the bankruptcy of the less efficient. (9, 282-83)

The central problem here, especially "when the time required for [disequilibrium] adjustments is long" (9, 284) -- is that orthodox theory incorporates only one dimension of the competitive struggle -- the benevolent **state** of its final equilibrium position -- but ignores the destructive and path-dependent competitive **process** through which this state may be temporarily achieved. It "does not count the cost of the struggle, but looks only to the benefits of the final results which are assumed to be permanent". Orthodox theory omits "the cost and character of the competitive struggle itself" (9, 285). But a scientific analysis cannot leave out of its evaluation of unregulated competition, "the tendency for wealth to be distributed where it is not appreciated", and, if "we have the welfare of the giraffes at heart, we must not overlook the sufferings of the shorter necks who are starved out" in the struggle, or the "overfeeding" of the winners, or the "evil look of anxiety" on the faces of the losers, or the "struggling greediness which overcasts the mild faces of the herd" (9, 285).

Most important, we must take into account the value of the productive resources destroyed in the competitive process -- of "the sweet leaves which fall to the ground and are trampled underfoot in the struggle" (9, 285). The maldistribution of income and wealth and the destruction of productive resources impart a destructive character to the competitive struggle that

laissez-faire does not take into account. For Keynes, this was not solely a theoretical problem: the real-world "costs" of ruthless competitive processes greatly troubled him as he examined the unemployment, excess capacity, inefficiency, and unnecessary human suffering in the depressed export industries in the mid 1920s.

Thus, in the new era a more powerful micro and macroeconomic role for the state will be essential. The central task of the moment is:

to determine what the State ought to take upon itself to direct by the public wisdom, and what it ought to leave to individual exertion. ... Perhaps the chief task of economists at this hour is to distinguish afresh the Agenda of government from the Non-Agenda; and the companion task of politics is to devise forms of government within a democracy which shall be capable of accomplishing the Agenda. (9, 288)

Keynes first asks: what are the appropriate institutional forms through which a democratic government can exercise an unprecedented degree of economic control over a capitalist system? Here he emphasizes the increasing importance of the **public corporation**. He believed that "public concerns" operating under general guidelines set by the government, but independent of the state in their day-to-day operations, would become ever more important in the new era, though he strongly opposed the detailed central planning of industry favored by many of the Labour Party's "State Socialists". According to Moggridge, Keynes believed that the public concern was likely to become "**the typical unit of industrial organization in Britain**" (1992, 267).

Thus, public and semi-public enterprises were to be the foundation of the new system, and "semi-autonomy" its key organizational or administrative concept. The state would set goals for these corporations and evaluate their performance, but not manage them directly.

I believe that in many cases the ideal size for the unit of control and organisation lies somewhere between the individual and the modern State. I suggest, therefore, that

progress lies in the growth and the recognition of semi-autonomous bodies within the State -- bodies whose criterion of action within their own field is solely the public good as they understand it, and from whose deliberations motives of private advantage are excluded, though some place it may still be necessary to leave, until the ambit of men's altruism grows wider, to the separate advantage of particular groups, classes, or faculties -- bodies which in the ordinary course of affairs are mainly autonomous within their prescribed limitations, but are subject in the last resort to Parliament.

I propose a return, it might be said, towards medieval conceptions of separate autonomies. But, in England at any rate, corporations are a mode of government which has never ceased to be important and is sympathetic to our institutions. (9, 288-89)

The historian Pollard noted that the Public Corporation enjoyed general support and roused widespread interest as a new administrative device in Britain in the interwar years (1983, 107).

A large share of industry and transport was, even in the 1920s, not controlled by private industry at all, but by various forms of public or non-profit-making organisations, and their growth is one of the most significant aspects of the period. (1983, 99)⁵

Indeed, according to Pollard, the increasing importance of the economic assets subject to the control of central and local governments and other public authorities during the interwar years represented "a distinct phase in the economic development of this country" (99).

Keynes then argues that an increasing percent of the country's largest and most important private companies are evolving toward a status that could make them as easy to regulate as public corporations. He calls attention to:

the trend of joint stock institutions, when they have reached a certain age and size, to approximate to the status of public corporations rather than individualistic private enterprises. One of the most interesting and unnoticed developments of recent decades has been the tendency of big enterprise to socialize itself. A point arrives in the growth of a big institution -- particularly a big railway or big public utility, but also a big bank or a big insurance company -- at which ... the shareholders, are almost entirely disassociated from the management, with the result that the direct personal interest of the latter in the making of profit becomes quite secondary [and] the direct interest of the management often consists in avoiding criticism from the public and from the customers of the

concern. This is particularly the case if their great size or semi-monopolistic position renders them conspicuous in the public eye and vulnerable to public attack. (9, 290)

To fully appreciate Keynes's mind set at this time it is essential recall that the 1920s and 1930s in Europe saw a powerful trend toward industrial self-regulation by monopolies, cartels, combinations and trade associations: this trend dramatically affected Keynes's position on industrial policy. Many firms, Pollard explains:

while nominally independent, were being combined frequently in their own, but sometimes even in different industries in complex ways inadequately described as 'lateral' or 'diagonal' integration. The links between the firms forming a group were sometimes economic or technical, but often they were little more than financial. Holding companies or subsidiaries were the most common means of control, but there were also inter-locking capital holdings, frequently unknown to the public, and inter-locking directorates.

...

Many of these trade associations collapsed in the slump of 1921-2, but in **the 'rationalization' movement of 1924-29**, much of it Government supported, others were formed. By the late 1930s there were probably 1000-2000 in existence in manufacturing alone, with a similar number to be found in distribution and other spheres. Most of them were driven sooner or later to concern themselves with price fixing and control. ...

Some trade associations went further and approached those of the German-type cartel by controlling not only prices, but also output quotas or capacity. (1983, 101-03), emphasis added)

The end result, according to Pollard, was that:

Monopolistic combination of one kind or another became much more common during the inter-war years, to the extent that by the end of the period **restrictive practices had become the normal framework of economic life**, buttressed as they were by associations, agreements and Acts of Parliament. (103-04, emphasis added)

Keynes was well aware of these developments and "welcomed the 'aggregation of production' as tending to stabilise the economy" according to Skidelsky (1992, 227). But acceptance of this trend implied support for increased government regulation of industry. Therefore, a "new partnership had to be established between the government and the private sector **to match the growing corporatism of industry**" (Skidelsky, 1992, 231, emphasis added). Since key decisions were already being made by conscious administrative judgement,

the groundwork had been laid for government planners to involve themselves in industry decision-making. Keynes central point was that the emerging importance of the system of public and semipublic corporations and associations combined with the evolution of collusive oligopolistic relations in the private sector already provided the foundation for a qualitative increase in state control of the economy. He believed that:

an interconnected elite of business managers, bankers, civil servants, economists and scientists, all trained at Oxford and Cambridge and imbued with a public service ethic, would come to run these organs of state, whether private or public, and make them hum to the same tune. (Skidelsky 1992, 227-28)

Thus, a vast new wave of nationalization, as called for by the Labour Party, was not a precondition for effective national economic planning.

The battle of Socialism against unlimited private profit is being won in detail hour by hour ... We must take full advantage of the natural tendencies of the day, and we must probably prefer semi-autonomous corporations to organs of the central government for which ministers of State are directly responsible.

I criticize doctrinaire State Socialism, not because it seeks to engage men's altruistic impulses in the service of society, or because it departs from laissez-faire, or because it takes away from man's natural liberty to make a million, or because it has the courage for bold experiments. All these things I applaud. I criticize it because it misses the significance of what is actually happening... (9, 290)

In "Am I A Liberal" (1925) Keynes associates himself with the American institutional economist John R. Commons's view that Europe and America were currently in transition to a radically new political-economic regime. According to Skidelsky, Commons was:

an important, if unacknowledged, influence on Keynes. Indeed, Keynes wrote to him in

1927 that 'there seems to me to be no other economist with whose general way of thinking I feel myself to be in such general accord'" (1992, 229).

Commons based his analysis of the new era on the demise of free competition and on the growing trend toward industrial self-regulation. Keynes tells us that Commons divides history into "three epochs" or "three economic orders."

The first is the era of scarcity... In such a period 'there is the minimum of individual liberty and the maximum of communistic, feudalistic or governmental control through physical coercion'. This was ... the normal economic state of the world up to (say) the fifteenth or sixteenth century.

Next comes the era of abundance. 'In a period of abundance there is the maximum of individual liberty, the minimum of coercive control through government, and individual bargaining takes the place of rationing.' ... [I]n the nineteenth century this epoch culminated gloriously in the victories of laissez-faire and historic Liberalism. ...

But we are now entering on a third era, which Professor Commons calls the period of stabilisation, and truly characterises as 'the actual alternative to Marx's communism'. In this period, he says, 'there is a diminution of individual liberty, enforced in part by governmental sanctions, but mainly by economic sanctions through concerted actions, whether secret, semi-open, open, or arbitrational, of associations, corporations, unions, and other collective movements of manufacturers, merchants, labourers, farmers, and bankers'.

The abuses of this epoch in the realms of government are Fascism on the one side and Bolshevism on the other. [State] Socialism offers no middle course ...

The transition from economic anarchy to a **regime which deliberately aims at controlling and directing economic forces in the interests of social justice and social stability**, will present enormous difficulties both technical and political. I suggest, nevertheless, that **the true destiny of the New Liberalism** is to seek their solution. (9, 304-05, emphasis added)

The central message in these essays is unmistakable. The era of economic coordination through atomistic competition is over. The new epoch requires a qualitative increase in the power of the state to "control and direct economic forces" both at the industry and macroeconomic levels, a "middle-way" revolution in economic and political organization that

avoids the inefficiency and immorality of laissez-faire as well as the political dangers of Fascism or Communism.

"The next step forward", Keynes concluded, "must come, not from political agitation or from premature experiments, but from thought" (9, 294). "A party programme must be developed in its details, day by day, under the pressure and stimulus of actual events" (9, 306). In July 1926, Lloyd George financed the Liberal Industrial Inquiry, a detailed study of the British economy by the Liberal Party. This was precisely the kind of careful, well-researched policy study Keynes thought essential.

III. Keynes and Industrial Policy: Coal, Cotton and the Rejection of Atomistic Competition

From 1926 through 1928 Keynes engaged in a detailed study of key British industries. Some of his most important observations about industrial organization are contained in a lecture to Liberal Party candidates in 1927 titled "Liberalism and Industry". Anarchic competition, he tells them, is an economic disaster.

In fact, under modern conditions the wastes and expenses of cut-throat competition and the beggar-my-neighbor business, which we used to applaud so whole-heartedly, are so devastating that every go-ahead and prosperous industry spends half its time trying to get rid of them; and those industries which still persist in small units and free competition -- like coal and cotton, to take two prominent examples -- are rapidly going bankrupt and will continue to go bankrupt until they alter their ways. (19, 642)

Coordination through competition must be substantially replaced by private-sector industrial self-regulation under state guidance.

Combination in the business world, just as much as in the labour world, is the order of the day; it would be useless as well as foolish to try to combat it. Our task is to take advantage of it, to regulate it, to turn it into the right channels. (19, 643)

What is needed now is neither free-market competition nor quantitative central planning but "regulated competition" (19, 643). The government:

must also be prepared to experiment with all kinds of new sorts of partnership between the state and private enterprise. The solution lies neither with nationalisation nor with unregulated private competition; it lies in a variety of experiments, of attempts to get the best of both worlds.

In England there have been made already without due recognition a good many experiments in that direction. ... The Government must recognise the trend of soundly run business toward trusts and combines. It must be prepared to recognise their existence as beneficent institutions in right conditions; and it must adopt an attitude towards them at the same time of encouragement and regulation. (19, 645)

Of course, the Liberal Party had historically been associated with hostility to trusts and combinations. But this is:

a wrong policy in modern conditions. It should be not discouragement, but encouragement for [trusts and combines] to live and exist in right conditions conducive to the general welfare. So far from their being any natural incompatibility between [combination and the general welfare], I believe that these great concerns run by salaried persons with a sufficient degree of decentralisation may, if they are handled by politicians and statesmen in the right manner, become a pattern and model of the way in which the world of the future will get the best both of large units and of the advantages that might be expected of nationalisation, whilst maintaining the advantages of private

enterprise and decentralised control. (19, 649)

Moreover, in the new era the state must also exercise substantial control over labor markets and the labor process.

It is not only in the direction of the regulation of capital that the state must be prepared for new functions. It must be prepared to regard the regulation of wages of great industrial groups as being not merely of private concern, and it must quite deliberately in its wages and hours policy treat the gradual betterment of the workers as the first charge on the national wealth... .. The problem of the education and the mobility of labour is going to be at least as important. ... It must be the concern of the state to know and have a policy as to where labour is required, what sort of training is wanted; and then where there are maladjustments, as there are in the coal industry, to work out plans for the transfer of labour from localities and trades where there is not demand to localities and other trades which are expanding and not declining. That is one example of the general policy which the Government has to be prepared for -- namely, the deliberate regulation from the centre in all kinds of spheres of action where the individual is absolutely powerless left to himself. ... I have given several examples of that, and as the machinery gets built up and the policy is developed, not a year will pass without an important addition to [these] spheres... (19, 646-47)

Keynes acknowledges that his vision of state economic planning is radically ambitious. It "is a vast programme that I have briefly outlined -- one of great practical and technical difficulty", but that is "**the** task lying to the hand of the new Liberalism" (19, 647, emphasis in original). He threatens to withdraw from the Liberal Party unless it pursues this "vast" program:

The conditions for me and for many others of sustaining any interest in party politics are, first of all, that my party should see the broad outline of this new industrial problem, [and] that it should be prepared to adopt an active policy towards it, and be ready to evolve new methods and an new attitude on the part of the state... (19, 647)

Fortunately, "an attempt is now being made to work out some first outlines of such a policy by the Liberal Industrial Committee, initiated by the Liberal Summer School and encouraged and supported by Mr Lloyd George" (19, 647).

Keynes wrote a number of articles dealing with the crisis in coal. He referred to coal as "an old-fashioned private industry which is not organised in combines and cartels" and suggested that if the owners refused to set up "a pool" through which "a scheme of quotas, of standard prices, and of penalties is drawn up", "the industry must disappear or it must accept nationalisation" (19, 528-29).

From late 1926 through 1928 he was also deeply involved in efforts to create a cartel in the American (or low-grade) section of the British cotton industry centered in Lancashire. Keynes became an adviser to and spokesman for the group of mill owners involved in this enterprise. Keynes's writings on Lancashire cotton describe the myriad ways in which disequilibrium competitive processes, which may take years or even decades to work themselves out, can preserve or exacerbate unemployment and excess capacity, and reproduce economic inefficiency.

The irreversibility of real capital accumulation is stressed. Small firms operating independently may do a decent job of adding capital to an expanding industry. However, an atomistically competitive structure is hopelessly inefficient at organizing the disinvestment

process needed in the declining industries. Free-market competition:

includes no provision whatever for reversing the process, except the slow and dragging cure which time brings at last by decay and obsolescence. (19, 590)

The permanent decline in export demand created the excess capacity troubling the cotton industry. Firms were forced to cut prices well below average costs to try and maintain some minimal degree of capacity utilization. Economists assume that such a price war is healthy because the least efficient producers are the first to be driven out of business. But this is often not the case. In the Tract on Monetary Reform (1923), Keynes stressed the importance of what he called the "**regime of money contract**" -- indebtedness now permeates the domestic and international economies. Since there has been a qualitative increase in the system's financial fragility, a fall in industry demand can easily trigger a wave of bankruptcies. However, the firms that are the first to be pushed into bankruptcy are not necessarily the least technically efficient, for debt is often incurred by innovative and aggressive rather than backward firms. "If this [price war] goes on for long, the mills which are financially weaker, though not perhaps technically inefficient, will become bankrupt". But even bankruptcy will not necessarily solve the problem of excess capacity.

The spindles of the bankrupt mills will not cease to exist. They will be sold at a low price and thus transferred into stronger hands on terms which will enable the competition to persist in conditions too severe for other businesses to earn their interest charges. And so the losses will continue until the gradual growth of demand over a long period or the obsolescence of the older mills restores the equilibrium at last. (19, 590)

The drive to stay in business leads firms to finance losses through new debt (which banks

supply in an attempt to keep their existing loans viable) and the run down of working capital.

This puts them in yet more desperate straits.

Excessive competition, resulting from excess capacity, has, in many cases, brought down the level of profits below that of interest charges and other unavoidable outgoings. The resulting losses have been provided out of bank loans and other resources which ought only have used as current working capital. The consequence is that the normal borrowing capacity of the industry has been exhausted in meeting losses, and is not available for new capital. In short, the spinners as a class, are frightfully hard-up, which leads to the pest of what is known as 'weak selling' [in which the need to pay the bank and buy new raw materials] carries the trouble a stage further and leads to prices which are worse than closing down. (19, 597-98)

This "involuntary selling by financially necessitous mills" carries competitive pressure on price to totally irrational and destructive levels.

What should be done? The only way to quickly eliminate excess capacity and shift production from the less efficient to the more efficient mills is through:

the cartel, the holding company, and the amalgamation ... By these means, and by these means only, can the surplus capacity be withdraw from competition and held in reserve against future requirements, so that the rest of the industry can earn normal profits meanwhile. (19, 591)

It was Keynes's belief, then, that the State had two new micro-oriented tasks: to assist firms in anarchically competitive industries to create associations and combinations; then to regulate and coordinate their interactions in the national interest.

IV. Keynes and "Britain's Industrial Future" -- 1928

In February 1928, the Liberal Party's Industrial Inquiry group published Britain's Industrial Future (BIF). The record is unclear as to the precise role played by Keynes in the creation of this collective work, but it is clear that he was a -- and probably **the** -- major force behind it. According to Harrod, "Keynes' contributions were of central importance" (1951, 392).

We know that he worked intensely on BIF for a year and a half, was a member of the Inquiry's Executive Committee, was Chair of the Committee on Industrial and Financial Organisation, drafted Book 2, wrote two chapters of Book 5 and collaborated on the other two, was in total sympathy with the Lloyd George orchestrated Book 4, co-authored the "Summary of Conclusions" section, and went over the draft as a whole.⁶ We also know that he was pleased with the policy agenda laid out in BIF. In a letter to H. G. Wells he wrote that BIF is:

a pretty serious effort to make a list of the things in the politico-industrial sphere which are practicable and sensible. It may therefore have a good deal of influence on future political programmes, whether or not there is a Liberal Party to put the matter through.
(in Skidelsky, 1992, 265)

For our purposes the most important aspects of BIF are that it: (1) supports Keynes's proposal for large-scale public investment as the centerpiece of macro policy, and provides for the first time detailed institutional proposals for the >socialization= of investment; and (2) elaborates an ambitious state-guided, corporatist industrial policy which, it appears, met with Keynes's approval. For Keynes in the 1920s, radical changes in macro and in industrial policy were complementary and essential requirements for the restoration and maintenance of full-

employment.

1) Public Investment as the Cornerstone on Macro Policy

In Book 2 Keynes demonstrates that public concerns over which the state already has direct or indirect control are, in the aggregate, so large that no substantial increment through nationalization is required to give the state effective control of the national capital accumulation process.

In a chapter on "The Public Concern" Keynes presents crude estimates of the amount of capital controlled by Britain's public and semi-public enterprises. His conclusion, previously stressed in a 1927 speech to the Liberal Party Summer School, is of the utmost importance.

Thus productive undertakings, mainly transport and public utilities, representing a capital in the neighborhood of , 2,750,000,000, or , 4,000,000,000 if we include roads, are already administered according to a variety of methods, all of which depart in some respect from the principles of private capitalism and unrestricted individualism. The transportation undertakings and public utilities included in this total, measured by the amount of capital involved, **must compromise at least two-thirds of what could be called the large-scale undertakings of this country**, though it would be a smaller proportion, measured in terms of the number of workmen employed.

...

These formidable totals -- amounting to over , 4,000,000,000 under all heads --

demonstrate what we have said above as to the unreal character of the supposed antithesis between Socialism and Individualism. What does the Socialist think he could gain by assimilating all this valuable diversity, developed by experience to meet real problems and actual situations, to a single theoretical model? Are not the abuses of private capitalism and unrestricted individualism capable of being reformed, in so far as they are still to be found in these mixed types, by a further evolution along the lines already set?

On the other hand, is the individualist really prepared to scrap all this elaborate special legislation by Governments of every political complexion under pressure of actual

circumstances, and hand over the vast capital of our public utilities and railway system to the operation of uncontrolled individualism? If not, then there is no question of principle at stake but only on of degree, of expediency, of method. (1928, 74-75, emphasis added)

Keynes argues that when this huge and diverse set of undertakings is brought under the coordination of the new and powerful **Board of National Investment** (proposed later in Book 2), the state will be able to regulate the aggregate rate of growth of the economy by controlling the pace of public capital accumulation, and direct investment toward the industries and areas hardest hit by structural unemployment.

The Board was to control all the financial capital made available to public and semi-public concerns. It could borrow on its own account and was even authorized to lend to private companies. Keynes estimates that it would control about 4 per cent of GDP a year to start, and up to 8 per cent of GDP in the foreseeable future. Thus, in the Board of National Investment Keynes proposed an institution capable of organizing and implementing the program of public capital accumulation he first espoused in 1924. His enormous optimism about its potential economic impact indicates how important this new approach to macro policy was to him. It would create:

with the least possible disturbance, an instrument of great power for the development of the national wealth and the provision of employment. **An era of rapid progress in equipping the country with all the material adjuncts of modern civilisation might be inaugurated, which would rival the great Railway Age of the nineteenth century.**

(114, emphasis added)

Lloyd George's Book 4 complements Keynes's work by presenting an ambitious list of specific

public investment programs for the Board of Investment to finance.

Those sections of BIF with which Keynes is associated present a wealth of detail about the structure, function and mission of the National Investment Board. **BIF thus provides conclusive proof that the "socialisation of investment" was not just a rhetorical device used to liven up Chapter 24 of The General Theory.**⁷ By the late 1920s it had become a **cornerstone of Keynes's approach to macro policy.**

2) Micro-Economics and Industrial Policy in the New Era

Book 2 also addressed industrial policy, though not in any systematic way. Let firms grow large, Keynes advised, then assist them to combine and collude. Some will eventually be absorbed into the system of public concerns. Those that retain private status must be regulated by the state.

Book 3, "Industrial Relations", contains a detailed proposal to restructure state-industry interaction. However, interpreting Keynes's attitude toward Book 3 is controversial. There is no evidence that Keynes was significantly involved in its writing (though he was Chair of the Committee on Industrial and Financial Organization).⁸ However, its enthusiastic support of corporatist structures reflects the direction of Liberal Party thinking in this period and is consistent with Keynes's approach to the firm and industry level problems of the era as revealed in his lectures and articles. Moreover, there is no evidence of any kind that he objected to the mode of industrial policy proposed here.

The Book's key chapter, "A Programme of Industrial Co-operation", opens with the assertion that Britain is "already advancing towards a new industrial order, though its outlines are still cloudy", then proceeds as follows:

This new order may be described as a system of industrial self-government under the regulation and encouragement of the State. It is the business of the statesman to perceive the direction of movement, and to guide and assist it. (205, emphasis added)

The first task is to "create the machinery of organised co-operation in the individual factory or workshop". To make the worker feel that "he is treated as a partner and not as a mere tool," (238) it proposed that every firm be legally required to form a "Works Council" to facilitate "permanent, regular, and established methods of consultation [between management and labor] in every factory and workshop of substantial size" (472). Book 3 mandates profit-sharing, and looks in the longer run to increasing ownership by workers to develop an institutional partnership between labor and management.

The skeleton of the proposed structure of cooperative labor-management-state decision making at the industry level and above is stated quite clearly in the summary of Book 3's core chapter.

It is the aim of Liberal Policy to bring about the establishment in every industry of a representative regulating body, including both employers and workers, for the consolidation of common interests, and endowed with the power of obtaining, under proper legal safeguards, legal sanction for their agreements.

This involves (a) the improvement of existing negotiating machinery; (b) the provision of adequate knowledge of the financial facts; and the provision of better machinery for central guidance, particularly by the creation of a **Ministry of Industry**, including the powers of the present Ministry of Labour, and of a representative **Council of Industry** working in close association with the Ministry. (468, emphasis added)

The main goal here "is the substitution of an organised system of co-operation for the existing system of conflict" and competition (210-11). To achieve this, "central guidance" is

required. This is the nub of the matter. Some new system of coordination must be designed, not just as a regulator of relations between capital and labor or among firms within an industry, but as the regulator of relations among industries and sectors within the economy as a whole. **BIF places its ultimate hope on a full-fledged corporatist structure in which one great council of industry-as-a-whole attempts self-regulation under the guidance and, ultimately, the control of a single powerful government Ministry.**

In the first place, continuous administrative action is necessary, through a properly organised department of State. In the second place, it would seem to be essential that **there should be some organ representative of industry as a whole**, to afford leadership and stimulus in the development of the machinery of co-operation, **to keep continuously in mind the interaction of industries one with another**, and ensure that the direction of industrial policy in this field shall not merely be political or bureaucratic in character. (220, emphasis added)

The responsibility of the Ministry of Industry is to help "British industry find its way to [labor] peace and to efficiency -- the two things are mutually dependent" (220). It will support, regulate and, where necessary, discipline integrated councils of self-regulating industrial groups.

In short, it should be responsible for whole system of State regulation of the conditions under which industry is carried on, and for all those activities in which the State finds itself brought into relations with the great organisations of employers and workpeople whereby industrial conditions are regulated. These functions are all so closely inter-related that they cannot be usefully separated; and the functions which the State has to perform in regard to industry cannot be well performed until [the industries themselves]

are properly co-ordinated. Thus reconstructed, **the Ministry would become one of the greatest offices of State, as it ought to be.** (221, emphasis added)

The Ministry of Industry can only be effective if and when "the great organisations of employers and workpeople" have themselves created (with State assistance where required) an effective structure to coordinate intra- and inter-industry activity through self-regulation. It should be regarded as one of the primary duties of a Minister of Industry to assist and forward industrial efficiency, not by overriding or disregarding the organised bodies of employers and workpeople, but by bringing them together and working with them. (222)

What institutional form should industry self-regulation take? Some members of the Liberal Industrial Inquiry were "strongly attached" to a proposal for "the formation of one large **National Industrial Council**, representative of the whole of industry" (224). However, at the present time, when a substantial base of experience in industrial self-regulation has yet to be established, a majority:

are agreed that a smaller and more workmanlike Council, such as we have defined, working in intimate relation with a reorganised Ministry [of Industry], would be able to perform many of the most useful functions of the larger body, as well as some others which would be beyond its reach.

These proposals, however, should in no way impede the establishment of a National Industrial Council on the amplest scale when industry is more fully organised and when the practice of co-operation is more widely established. (225)

For the intermediate future, then, Book 3 proposes the establishment of a Council on Industry to self-regulate and self-coordinate, under the guidance of the Ministry of Industry, both intra- and inter-industry activity in the new era of British corporatism.

It would, however, be undesirable to leave the functions of guiding and stimulating industry into new courses wholly to a public department, however well organised. Industry itself must provide leadership. Industrial policy must be safeguarded against those sudden reversals which are apt to follow changes of Government, and against any risk of a too rigid bureaucratic method. For these reasons we recommend that the new Ministry of Industry work in association with a statutory Council of Industry, which should be so constituted as to represent, and to command the confidence of, the industrial world. ... We suggest that it should consist of nine representative employers and of nine representatives of organised labour, selected by the Government from a panel nominated by representative bodies of employers and wage-earners; and that there should also be six other members directly appointed by the Minister. (222)

The Council of Industry was to be given important responsibilities and powers.⁹ The creation of this Council would "be a very material contribution to the development of industrial self-government" (224). If and when it has proven its worth in this regard, a path will have been cleared for the creation of the ultimate corporatist institutional arrangement -- one great "National Industrial Council" to self-regulate "the whole of industry" under the watchful eye of the state's Ministry of Industry.

V. Did Keynes Become More Conservative in the 1930s and 1940s?

The changes Keynes envisioned in the economic role of the state in this period are so significant that it might not be unreasonable to call them 'revolutionary', provided we keep in mind that they were intended to be accomplished peacefully, working through Britain=s existing

political processes. Keynes was proposing a dramatic transformation in the economic power of the State, to be brought about not by mass political agitation from below, which he feared, but by elite consensus from above -- a gentlemen's revolt.

But were these radical ideas just passing fancies, to be shed in his more mature and, supposedly, more conservative years?

With respect to macro policy and the central role of public investment the answer is a definitive no. Keynes repeated his belief that a major program of large-scale public investment was the key to sustained prosperity over and over again: in 1929 in "Can Lloyd George Do It?", in 1933 in "The Means to Prosperity", in 1936 in The General Theory (with its call for "a somewhat comprehensive socialisation of investment" and Keynes's assertion that he "expects to see the State ... taking an ever greater responsibility for directly organising investment"), and in his government work during World War II on wartime planning and the post-war economic order. In 1943 he said that "if the bulk of investment is under public or semi-public control and we go in for a stable long-term programme, serious fluctuations are enormously less likely to occur" (27, 326).¹⁰

The question of his attitude toward competition and industrial organization and policy in later years, however, is harder to answer. Though he continued to express support for specific industrial policies, such as state-directed credit allocation and industrial location programs, to the best of my knowledge he did not write at length or in depth about industrial policy after the late 1920s.¹¹ The start of the "Great Slump" in late 1929 shifted the focus of his attention from questions of industrial policy to problems of deficient aggregate demand. By 1930 his thoughts were focused on combating mass or generalized, as opposed to structural, unemployment. And

by 1937 or so, he was confronted with the prospective problems of the war economy as a result of Britain's military buildup. However, again to the best of my knowledge, Keynes never explicitly rejected the views on competition and industrial policy we examined in the body of this essay.¹²

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ENDNOTES

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1. References to Keynes's Collected Writings will list volume and page number respectively.
 2. See, for example, Kregal (1985) and Brown-Collier and Collier (1995).
 3. Joan Robinson reported the following quote from a colleague of Keynes: "Maynard had never spent the twenty minutes necessary to understand the theory of value. On these topics he was content to leave orthodoxy alone" (1962, 79).
 4. While Skidelsky briefly mentions the arguments Keynes presents here, he fails utterly to appreciate their significance.
 5. Pollard states that:

Among the most important of the [public and semi-public concerns] were the co-operative societies, registered under the Industrial and Provident Societies Act, and the building societies, registered under the Buildings Societies Act; enterprises administered by charitable, educational and similar bodies; local authorities, administering over one-third of the gas works, two-thirds of electricity supplies, four-fifths of water supplies and of tramway mileage, virtually all the trolley-bus systems as well as a large proportion of omnibus and other services. There were, further, ad hoc authorities such as dock and harbour boards, including those of London, Liverpool and Glasgow, and the Metropolitan Water Board, established in 1902; companies established by Act of Parliament, mainly in the public utilities field, including the railways; enterprises administered directly by the State, including the Post Office, the dockyards, and the Crown Lands; and the Public Corporations. In 1928 the Liberal Industrial Inquiry found that the capital administered

by these authorities came to about , 4 billion (including , 1.3 billion for roads and , 1.15 billion for railways) and was thus of the same order of magnitude as the aggregate capital of all joint-stock companies (1983, 99-100)

6. See Harrod (1951, 392-93); Moggridge (1992, 457-59); and Skidelsky (1992, 264-69).

7. The idea that Keynes's reference to the socialization of investment in Chapter 24 was an unimportant obiter dictum is almost universally held. For example, James Galbraith and William Darity Jr., two outstanding economists, write in their macroeconomic textbook:

There is no evidence to suggest that Keynes promoted his proposal for socializing investment, and it only surfaces briefly in the latter pages of The General Theory. (1994, 54)

8. A major reason why it is difficult to pin down Keynes's precise relation to this and other areas of BIF is that the records documenting the creation of BIF are very sparse.

9. Pages 223-24 enumerate a number of important responsibilities ceded to the Council on Industry.

10. It should be noted that from the mid 1920s until his death, Keynes supported strong controls on the movement of capital across Britain's borders as a necessary condition for an effective program of public capital accumulation and sustained full employment.

11. One clear exception is his series of proposals in the 1930s and 1940s in support of the creation and control of buffer stocks of raw materials and primary products by national governments and international organizations to eliminate the enormous instability in prices and output created in these markets by the inefficiencies of competitive processes.

12. It is true that in chapter 24 of The General Theory Keynes argues that the main problem in the laissez-faire economy is not to be found at the firm or industry level; when aggregate demand is appropriate, markets allocate resources with reasonable efficiency. This might be considered to be a change from the position he took in the 1920s.

However, this chapter is notoriously tricky to interpret because in it Keynes is trying to accomplish two objectives that are at cross purposes. On the one hand, he is reminding his reader of his radical vision of middle way planning. For example, the state is to socialize investment and determine the level of national income, the income split between consumption and saving, the division of investment between foreign and domestic uses, and the distribution of income. It is also supposed to eliminate over time the function of the rentier.

On the other hand, he is trying to convince his fellow economists, on the whole a conservative lot, to support his radical crusade. This may well have led him to try to convince

his readers that his message was not really as radical or threatening to the existing order as it might seem at first glance.

Perhaps in his praise of the allocative efficiency of markets in this chapter, one can detect the residue of the sugar-coating he sprinkled on his radical message to help make it more palatable to his conservative colleagues. As Minsky put it, in The General Theory Keynes conceded much to the Classical school in part because he was consciously opportunistic. He cites Keynes's desire to speed the adoption of correct policy, if not of correct analysis... (1975, 13).