

Marx, Keynes, and Minsky on the Instability of the Capitalist Growth Process and the Nature of Government Economic Policy

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In his essay in this volume, Hyman Minsky is hunting big game. As he tells us in his opening paragraph, he is attempting to explain the recurrent crises in the domestic economy and in the international financial system, as well as the failure of economic policy either to prevent the outbreak of these crises or to eliminate them in reasonably short order. He also presents a sharp critique of received economic theory as a reliable guide to policy. Toward the end of the paper, Minsky suggests some fundamentally new directions for government policy, and he calls for the radical restructuring of economic policy institutions. In the spirit of this occasion, Minsky draws heavily on the work of John Maynard Keynes, both in his analysis of the current economic crisis and of the inadequacy of policy and in his suggestions for institutional change.

In keeping with this same spirit I will draw upon the ideas of Keynes and Marx in addressing the major issues and questions posed by Minsky. In this essay I will compare and contrast theories of cyclical and long-term instability associated with the Marxian tradition and with the work of Keynes and Minsky. I will assess the explanations of the ongoing economic crises of the current era offered by Minsky and by Marxist writers. I will also discuss the different perspectives that the Keynesian and Marxian traditions bring to the analysis of the economic role of government.

Before getting down to business, however, I would like to express the opinion that Hyman Minsky is one of the most interesting and important macro economists to have written about the postwar era. When the mainstream of the profession was almost unanimous in celebrating the death of the business cycle and the onset of perpetual prosperity in the mid-1960s, Minsky reminded us of the endogeneity of cyclical instability and of the transitory nature of the institutional underpinnings of financial markets. The economic crisis of the 1970s and 1980s and the crisis of economic theory and policy that accompanied it may have come as a surprise to most of the profession, but Professor Minsky would have been surprised if such crises failed to materialize. I have, indeed, learned a good deal from Minsky's writings on the workings of the macroeconomy.

Minsky and Keynes on the Cyclical Instability of the Capitalist Growth Process

Inspired by Keynes, Minsky focuses his analysis of cyclical instability on the centrality of the investment decision in the capitalist growth process and on the key role played by financial institutions and practices in influencing the decision to invest in physical capital in the mature capitalist economy. Keynes, of course, analyzed the investment decision by means of a comparison between the marginal efficiency of investment (MEI), an index of the expected rate of profit, and the long-term rate of interest. The calculation of the MEI itself involves a comparison of the *expected* net cash flow over the *expected* life of the investment good with the cost of that good. Therefore, the determinants of the MEI include the cost (or supply price) of the capital good, all those factors that influence the entrepreneur's forecasts of future revenues and costs over the expected economic life of the investment, and the confidence that the entrepreneur places in the reliability of his forecasts.

Using these concepts, Keynes constructed his theory of the potential volatility of investment and of the potential instability of the capitalist growth process. Keynes's theoretical structure is, at least in principle, quite complex because anything that alters the expected future costs or revenues of an enterprise has an impact on investment. Thus, expected future changes in capital-labor relations, in the labor process, in technology, in labor productivity, in the organization of the enterprise, in the degree of domestic or international competition, in the general state of demand for products and services (and therefore in aggregate demand), in financial markets, in government policy, in the cost and reliability of foreign sources of raw materials, or in the condition of foreign markets will affect the expected rate of profit on investment and the degree of confidence with which the expectation is held. Any of these changes will therefore affect the level of investment. Note carefully that, for Keynes, many of the key determinants of investment spending are real, not financial, variables.

Keynes moved some of these variables center stage; others he moved out of the spotlight. In spite of the central role Keynes gave to real sector determinants of costs, revenues, and the profit rate in the theoretical constructs he developed to analyze investment, real sector variables are deemphasized in much of his work, a point to which I return below. The unknowability of the future, on the other hand, is given a starring role. The formulation of expectations, the importance of confidence, and the volatility of both are major characters in his story. Most important for my purposes here, financial markets receive star billing for two distinct reasons. First, the cost of borrowed funds is obviously an important determinant of investment. Second, Keynes argues—especially in chapter 12 of the *General Theory*—that financial markets will inevitably be affected by

waves of optimism and pessimism and that these waves will in turn impinge upon entrepreneurs' calculations of the MEI. The volatility will be magnified through this channel.

The main themes and guiding insights of Minsky's work are heavily influenced by that part of Keynes's analysis stressed here. Minsky is well known for his financial instability hypothesis, the core of which can be stated rather succinctly.¹ Investment spending is the prime mover of the economy. *Ceteris paribus*, an investment boom is most likely to be initiated in a financially robust environment, that is, an environment in which firms are unencumbered by debt; financial and nonfinancial enterprises and households are in liquid condition; and interest rates are low. Once investment spending begins to take off, its rise will be self-enforcing to a large extent. In Minsky's model, increased investment always leads to larger current profits, and larger current profits stimulate expectations of higher future profits; these, in turn, will trigger more investment. Rising investment and profits will produce increasing confidence on the part of financial enterprises and individual wealth-holders; increased confidence will reduce liquidity preference and induce greater risk-taking because every specific act of financial investment will seem to the investor to entail less risk than it did before. Enterprises will make greater use of debt capital, banks will make more loans and riskier loans, and they will seek out increasingly expensive and volatile sources of funds; and households will decrease liquidity in an attempt to get rich quick. This situation has been referred to as "boom euphoria." It results in increasing illiquidity in the economy as a whole. Debt/equity and loan/deposit ratios rise, interest coverage ratios fall, and interest rates rise. The expected gross cash flows of all economic units become increasingly committed contractually to other units; the margin for error becomes proportionately smaller. The ability of most units to pay their bills in the face of an unexpected economic downturn declines. In Minsky's colorful phrase, an extended economic expansion eventually creates "financial fragility."

As financial fragility rises, the increasing interest rates that inevitably occur in a mature boom make a drop in investment spending increasingly likely. Once investment turns down in a financially fragile environment, financial markets accelerate the rate of descent. Lower investment than expected means lower aggregate demand, lower sales, and smaller profits than expected; the initial problem is then magnified by multiplier effects. Hard pressed to make interest and principal payments, individuals and enterprises are forced to sell relatively illiquid assets. The plunge in financial asset prices in turn makes real investment even less attractive. Should these intertwined

¹ For a relatively concise statement by Minsky of his financial instability hypothesis, see Minsky, 1982a. For a more extensive treatment see Minsky, 1975.

processes of declining investment and falling financial asset prices pick up enough steam, a debt-deflation crisis may occur unless a lender of last resort intervenes. The recession-depression and debt-deflation, in turn, eventually help recreate a financially robust environment, and the cycle is ready to reproduce itself.

Domination of the Real Sector by the Financial Sector in the Work of Keynes and Minsky

Minsky's work on financial aspects of the cycle fits rather nicely into a general Marxian approach to growth and instability, as I will explain in the next section. However, there is a major problem with Minsky's theory of capitalist instability as evaluated from a Marxian perspective: there are no real-sector sources of instability in his model. The explanation of the transitory nature of both expansion and contraction is located exclusively in financial markets. Indeed, the real sector as a semiautonomous sphere of economic activity and decision making comes perilously close to vanishing in much of Minsky's work. In his de-emphasis of real-sector determinants of instability, Minsky follows in the footsteps of Keynes. This analytical imbalance leads Minsky to a one-sided and therefore inadequate explanation of the crisis of the 1970s and 1980s.

There are two key building blocks in Minsky's work on capitalist instability: his theory of investment and his theory of profit determination. They also constitute the foundation for his conclusion that the financial sector is the exclusive source of instability in a capitalist economy. First, I will examine his theory of profit determination.

In the years since the publication of *John Maynard Keynes* (1975), Minsky has introduced a more formal model of profit determination into his analysis (see Minsky, 1982a and 1982b). He has adopted the theory of profit associated with Michal Kalecki and used in Cambridge growth models and Post-Keynesianism in general. "The great insight into the determination of profits in our economy that is associated with Kalecki," Minsky has argued, "is that profits arise out of the impact of the accumulation process on prices" (1982b: 11). In contrast with neoclassical price theory, which focuses on the price system as an (optimal) allocator of factors of production among competing uses, the Kalecki-Cambridge tradition sees the price system primarily as an income distribution mechanism that cuts the income pie into profit, wage, and interest shares. Since different economic classes are assumed to have different savings propensities, it is the price system that determines aggregate savings behavior in the economy. In this approach, capital accumulation (or investment) generates income while the price mechanism simultaneously determines the profit share of that income and the percentage of income that is saved. To investigate the potential for the development of instability in this section of Minsky's model, I first ask whether it can ever produce

a pace of accumulation that generates insufficient profits or savings to sustain itself. In anticipation of my conclusion, the answer is that it does not.

Minsky opens a discussion of the theory of profit determination in a recent paper as follows: "There is no need to repeat Kalecki's demonstration that gross profits = gross investment + capitalists' consumption" (1982a: 26). (He is referring to a simple Kalecki two-class model in which workers do not save, so that all saving comes from profits.) Now Minsky clearly treats this equation as if it were a traditional Keynesian "gross investment = gross saving" equilibrium condition. In fact, the Kalecki equation cited is a national income accounting *identity*. In the work referenced by Minsky, Kalecki (1971: 79) goes on to assume explicitly that planned investment and realized investment are equal at all levels of investment. It is thus a curious model in which gross saving adjusts automatically and instantaneously-almost magically-to balance any change in gross investment.² In other words, the Kalecki model upon which Minsky bases his profit determination theory is a super-equilibrating model where aggregate demand and supply are never out of balance: there is definitely no potential for instability here, the economy cannot attain even temporary disequilibrium.

Even though Kalecki has no equilibrating process in his equations, he obviously has one in his mind. To understand it, we need to consider his well-known mark-up theory of pricing (and income distribution), a theory to which Minsky subscribes. For Kalecki, the exogenous "degree of monopoly" determines the mark-up that corporations apply to prime unit costs to set prices; the mark-up determines the profit share of income. Under Kalecki's standard assumptions, the size of the mark-up is independent of the level of investment, output, and employment. In other words, the profit share of income remains constant even if the condition of the economy alters drastically.³ Therefore, every change in the level of investment will trigger changes in output and income. This must continue until profits-a fixed percentage of income-change by enough to make savings balance the new investment level. The equilibrating process that Kalecki has in mind, then, is simply a variant of Keynes 's multiplier dynamics (or vice-versa).

² As Don Patinkin (1982: 71) recently commented: "Kalecki ...is implicitly assuming that at every point in his investment cycle, planned saving and investment per unit of time have -in some unspecified manner- been equilibrated."

³ Cambridge growth models assume that the mark-up (and the profit share) rises when the pace of capital accumulation creates aggregate excess demand. This rise creates the extra profits and savings to justify the faster pace of capital accumulation and raises the ratio of investment to consumption in the economy.

While the addition of a mark-up pricing theory of income distribution provides an equilibrating process for Kalecki's theory of profit determination, it does nothing to alter the conclusion that there are no potential sources of instability in the real sector of Minsky's theory. On the one hand, any conceivable level of gross investment will generate an equal level of gross saving so that aggregate excess demand will be zero at every level of investment. On the other, the assumed constancy of the mark-up and profit share guarantees that the rate of profit on investment is likewise constant, no matter what the level of investment. In Minsky's theory of investment spending (discussed below), capitalists will continue to invest provided that the expected rate of profit on investment exceeds the cost of financial capital. This means that the high rate of investment of the boom can never initiate a chain of real-sector developments (such as rising raw materials prices, rising wages, falling rates of productivity growth, increased import competition, or market saturation) that lower the rate of profit and cause a decline in the rate of investment, production, and employment.

Minsky is quite emphatic about this last point. An investment decline (and resultant recession) can never be *initiated* by a prior decline in the expected profitability of investment; rather, it takes an initial drop in investment to induce a *subsequent* decline in profits. Investment and profits are not mutually codetermining; rather, investment spending calls the tune and profits dance accordingly. As Minsky puts it: "In the simplest Kalecki case, where aggregate profit equals aggregate investment, the shortfall of realized profits below anticipated profits requires a logically prior shortfall of investment. This leaves the question of ... crises and ... depressions unexplained, for it is the decline in investment that has to be explained" (1982a: 25).

In contrast to Keynes, who argued that capital accumulation led to a short-run and a long-run decline in the marginal efficiency of investment (see, for example, chapter 17 of *The General Theory*), Minsky can find no impediment to perpetual balanced growth in the real sector of the economy.⁴

I find the constant-mark-up Kalecki model of profit determination used by Minsky, as is evident by now, to be quite unsatisfactory. This model assumes cyclical and secular constancy in

⁴ Minsky's view is nicely summarized in the following quotation: "The gross profits of business depend not upon the 'productivity' of capital in any technical sense, but upon the amount of investment. The profitability of existing capital-and profit expectations-can only change if investment and expected investment [first] decline. Thus we have to look elsewhere-to arguments other than those derived from assumed properties of production functions and hand waves with regard to over-investment-to explain why the marginal efficiency of investment falls. The natural place to look within the Schumpeter-Keynes- Kalecki vision is in the impact of financing relations" (1983: 13).

the mark-up and the marginal efficiency of investment, the absence of any tendency for the rate of profit on capital to fall until after the expansion ends, and secular constancy in the rate of profit on capital.⁵ However, there is a substantial body of empirical evidence that suggests that none of these assertions is true.⁶ The bulk of this evidence demonstrates that there is significant cyclical variation in the mark-up and the profit share, and that the rate of profit turns down well before the end of the typical cyclical expansion and substantially earlier than plant and equipment spending, a lagging indicator.

Of central importance to an explanation of the crisis of the 1980s, the empirical evidence clearly suggests that the rate of return on capital in the United States reached a post-Korean War peak in 1965 or 1966, in the middle of the long boom of that decade, and it experienced a secular decline in the succeeding era. This secular fall in the profit rate began while the economy was still moving ahead with vigor; the rate of unemployment stayed below 4 percent for several years following its initial decline. Note that the falling profit rate that signaled the start of the era of secular crises was not preceded by a decline in investment. Indeed, real investment held up surprisingly well in the late 1960s; it took several years for investment spending to reflect the decline in the rate of profit.

⁵ There are Post-Keynesian mark-up pricing models that successfully integrate the concept of a constant mark-up with the existence of a cyclically (but not secularly) variable realized or observable mark-up. In these models firms are assumed to set price by applying a constant mark-up to "normal" or "standard" unit costs. Normal unit labor costs are defined as realized wages divided by average or trend labor productivity. Since realized labor productivity is quite variable cyclically, the models can incorporate or explain a cyclically variable realized mark-up. Note, however, that such models locate the cause of significant or extended declines in the profit share in discretionary corporate pricing policy. In other words, the persistent decline in profit share that occurred from 1966 through 1970 was imposed by the corporations on themselves as a matter of discretionary policy.

⁶ See, for example, D. Holland and S. Myers, "Profitability and Capital Costs for Manufacturing and All Nonfinancial Corporations," *American Economic Review* (May 1980): 320-25; G. Moore, *Business Cycles, Inflation, and Forecasting* (Cambridge, Mass.: Ballinger, 1980), pp. 288 and 294; Weisskopf (1979); R. Hahnel and H. Sherman, "Income Distribution and the Business Cycle," *Journal of Economic Issues* (March 1982): 49-74; D. Allman, "The Decline in Business Profitability," *Economic Review (Federal Reserve Bank of Kansas City)* (January 1983): 19-26; K. Pulling, "Cyclical Behavior of Profit Margins," *Journal of Economic Issues* (June 1978); W. Nordhaus "The Falling Share of Profits," *Brookings Papers on Economic Activity* 1 (1974): 169-216; M. Lovell, "The Profit Picture: Trends and Cycles," *Brookings Papers on Economic Activity* 3 (1978): 769-88; and Robert J. Gordon, "Inflation, Flexible Exchange Rates, and the Natural Rate of Unemployment," in *Workers, Jobs and Inflation*, ed. Martin Neil Bailey (Washington, D.C.: Brookings Institution: 1982).

As I read the data, then, the Minsky-Kalecki theory of profit determination is empirically implausible, and this implausibility has important theoretical consequences. To explain adequately cyclical instability and secular crises, a theory of the real sector that is consistent with this evidence is needed, a theory in which investment affects profits but profitability also adversely affects investment. We need a model of the real sector capable of generating profit rate behavior that is inconsistent with perpetual expansion.

Where, then, are the roots of instability in Minsky's model? The answer, quite obviously, is that they can only be found in capitalist financial institutions. To see this, one must examine his theory of investment. Minsky has a financial theory of investment; investment demand is determined in financial markets. Keynesian theory, Minsky states in his essay, "centers around a financial theory of investment and an investment theory of the business cycle."

In his book *John Maynard Keynes*, Minsky presents investment demand as a function of the difference between the demand and supply price of capital goods, a variant of the "MEI versus interest rate" criterion for investment decisions. The demand price is the present value of the future profits expected to be generated by a new capital good, and the supply price is the cost of producing the new capital good. (In the tradition of Kalecki, Minsky assumes a relatively constant supply price up to full capacity utilization in the capital goods industry.) What one might expect (and hope) to see as this supply-versus-demand price framework gets fleshed out is a theory in which investment is conceptualized as the outcome of an interaction between two partially autonomous sectors of the economy—the real sector (or industrial and commercial sector) and the financial sector. In these two sectors, one would presume, different agents and institutions (with objectives and constraints that are not totally identical) make decisions based on information sets that have some elements not held in common and on expectations that might be similar (and interactive), but are distinct nonetheless.

Such expectations and hopes are not ultimately met, however, because in Minsky's fully-developed model there is no relative autonomy for the real sector. Just as is the case in general equilibrium models of the macroeconomy, there is nothing that the decision makers in Minsky's industrial enterprise know (information), foresee (expectations and confidence), or desire (objectives) that is not fully and simultaneously known, foreseen, and desired by financial-portfolio holders. Since financial markets have the same expectations concerning the profitability of investment as industrial enterprises, and since they determine the capitalization factor used to convert profit expectations into a demand price for capital goods, it seems reasonable to conclude that in Minsky's theory the demand price for investment is essentially determined in financial

markets.⁷ Here is how Minsky states his position: “Share prices together with the market value of debt give us a market valuation of the bundles of capital assets collected in a firm. If the market value is high relative to the supply price of such assets newly produced, then presumably the pace of investment will be stepped up” (1975: 101). Elsewhere he argues that “the demand price of investment is derived from the [financial] market price of capital assets. The market price of capital assets depends on relations that Keynes identified under the rubric of liquidity preference” (1982: 29). It is important to bear in mind when interpreting this statement that Keynes’s theory of liquidity preference is a theory about the way in which wealthy individuals (or institutions) compose their financial portfolios.

For Minsky, then, the firm’s demand price for capital goods and the price of financial claims on the firm (its stocks and bonds) are virtually indistinguishable. Just as with the Keynes of chapter 12 of *The General Theory*, the real and the financial become conflated in Minsky’s work, and it is finance that steps in the spotlight, while the real sector fades into the wings.⁸ One is almost tempted to argue that the concept of the partially autonomous industrial enterprise could be replaced in Minsky’s investment theory by a telephone: one call to a stockbroker (to establish the market value of the firm) and one call to a contractor (to establish the replacement cost of the firm’s capital assets) should suffice to determine the firm’s investment spending program. In his book *John Maynard Keynes*, Minsky makes several summary comments about Keynes’s theory that apply just as well to his own. For example, he tells us that there is implicit in Keynes’s analysis

a view that a capitalist economy is fundamentally flawed ... because the financial system necessary for capitalist vitality and vigor... contains the potential for runaway expansion, powered by an investment boom. This runaway expansion is brought to a halt because accumulated financial changes render the financial system fragile, so that not unusual changes [especially rising interest rates] can trigger serious financial difficulties.

⁷ The reader should consult Minsky, 1975, chapters 4-6, to evaluate my judgment on this matter.

⁸ The theoretical conflation of the real sector and the financial sector (with one sector dominant) has several undesirable consequences. One is that change in the pace or direction of macroeconomic activity must always be initiated in one sector, then transmitted to the others. (For Keynes and Minsky the initiating sector is the financial sector; for most Marxists, it is the real sector.) This assumption does not seem to be consistent with empirical and historical evidence. When semiautonomy is preserved, impulses for change may originate in either sector or in both simultaneously, and complex, variable, and interactive lead and lag structures between the sectors are permissible. Another undesirable consequence of conflation is that it signals the theorist to confine his or her search for the roots of growth and instability to one sector or another.

... The fundamental financial attributes of capitalism mean that periodic difficulties in constraining and then sustaining demand will ensue. (1975: 11-12)

Somewhat later in that book he argues as follows: “In Keynes’s theory the proximate cause of the transition of each cyclical state is the instability of investment; but the deeper cause of business cycles in an economy with the financial institutions of capitalism is the instability of portfolios and of financial interrelations” (p. 57).

I might summarize my argument as follows. If Minsky’s theory of investment is motivated by expected profits, expected profits are substantially determined by realized profits and realized profits are, in turn, determined by investment. In this seamless real-sector model, every possible level of investment is self-perpetuating without limit. It is only financial fragility and the rising interest rates of the mature boom that permit its demise; real-sector determinants of investment profitability seen in isolation produce only perpetual growth. The ultimate or “deep” cause of capitalist instability in Minsky’s world is therefore to be found in the dynamics of capitalist financial markets. Given the fact that instability is the central focus of Minsky’s work, I think it fair to conclude that the real sector of the economy has no active, essential role to play in the fundamental behavioral processes of his theory.

Cyclical Instability: The Marxist Tradition

The relative strengths and weaknesses of the theories of cyclical instability put forth by Minsky and most Marxists are complementary. Minsky’s work emphasizes financial aspects of crisis generation but adds little to our understanding of the determinants of instability in the real sector. The traditional Marxist literature on accumulation and crisis, on the other hand, errs in the opposite direction: it focuses on the real sector almost exclusively. Marxists have had relatively little to say about financial aspects of either cyclical or secular instability. Interestingly enough, Marx himself did not give theoretical priority to production over finance in his treatment of crisis.

Marx’s abstract analytical framework for crisis theory combines financial and real analysis in a balanced way, as I have argued in detail elsewhere (1985). Indeed, Marx’s treatment of financial aspects of capitalist crisis is qualitatively similar to Minsky’s. Marx’s view of the role of financial phenomena in the accumulation process might be summarized as follows: financial intermediation is an important and often dominating accelerator and destabilizer of the growth process. Financial markets push the accumulation process forward in the upswing, driving it at a pace it could not otherwise attain, while they simultaneously give to the growth process the characteristic that Minsky calls fragility and Marx called ‘oversensitivity.’ In Marx’s scheme,

adverse economic developments which might cause only a mild and temporary hesitation in an ongoing expansion in the absence of an oversensitive financial environment can generate a crisis and collapse in its presence. Moreover, semiautonomous disturbances in the financial sector can themselves initiate a crisis if the system is oversensitive. And an overextended, oversensitive financial system can turn what might have been a mild downturn into a financial panic and depression.

If the reader is surprised because this sounds more like Minsky than the Marx with whom he or she is familiar, that is because most Marxists have neglected Marx's treatment of financial intermediation. The fact is that on this subject Marx *is* a lot like Minsky, and vice-versa. A few representative quotations from volume 3 of *Capital* will have to suffice here as evidence for this claim.

It is precisely the development of the credit and banking system which ... seeks to press all money capital into the service of production... that makes the entire [economic] organism *oversensitive*. (1981: 706, emphasis added)

In a system of production where the entire interconnection of the reproduction process rests on credit, a crisis must evidently break out if credit is suddenly withdrawn and only cash payment is accepted, in the form of a violent scramble for means of payment. (1981: 621)

[When the rate of profit falls,] this disturbance and stagnation paralyzes the function of money as a means of payment [of debt], which is given along with the development of capital and depends on ...presupposed price relations. The chain of payment obligations at specific dates is broken in a hundred places, and this is still further intensified by the breakdown of the credit system. ...All this, therefore leads to violent and acute crises, sudden forcible devaluations, and actual stagnation and disruption in the reproductive process and hence to an actual decline in reproduction. (1981: 363)

Minsky's work on financial markets, as I see it, is broadly consistent with Marx's unfinished effort to develop a sophisticated theory of finance that could be integrated with his analysis of production to form a general theory of growth and instability in the capitalist economy. Modern Marxists will find that Minsky (and Keynes) can help them in their own efforts to understand financial aspects of instability. On the other hand, Keynesians would do well to pay far greater attention to the contributions of the Marxian tradition toward the development of a theory of the real-sector determinants of cyclical and secular instability. These contributions have come about

in large part because the logical structure of Marxian theory roots capital accumulation so deeply in the real sector that it is difficult for someone working in this tradition to de-emphasize real-sector impediments to accumulation. To see why this is so, I briefly examine the basic structure of Marxian macrotheory.

Marxian macrotheory, at its most abstract level, starts from a general concept of the capitalist mode of production (or economic system), then moves to an analysis of what are called the “circuits of capital.” These are stages in (or, phases or aspects of) the process of profit making and the accumulation of capital. In circuit one, inputs (including labor and capital equipment) are purchased; in circuit two, these inputs are transformed (through the production process of the capitalist enterprise) into new commodities; and, in circuit three, the new commodities are circulated (or offered for sale).

The basic idea is that capitalists invest money capital in circuit one in the hope or expectation that an attractive rate of profit on their investment will be obtainable from the revenues realized in circuit three. Given the initial pace of investment, conditions in the three circuits determine the realized rate of profit. Profit rates below expectations slow the rate of accumulation because the mass of profits is smaller than anticipated (and because our disappointed capitalists may lose confidence and use a smaller percentage of their profits for productive investment), while an increasing realized rate of profit, on the other hand, speeds up the pace of accumulation.

The key point here is that the basic analytical framework of Marxian theory guides those influenced by Marx’s ideas to focus their attention on the variables stressed in the circuits of capital schema and, as I illustrate below, on the institutional foundation of the circuits. The most important of these macro variables are the primary real-sector determinants of the rate of profit, precisely those variables neglected by Minsky and Keynes. Issues of traditional concern in circuit one include the condition of labor markets (one aspect of which is the existence, character, and strength of labor unions) and determinants of the wage. Important considerations in circuit two include the organization of the enterprise, the choice of production technology and its embodiment in capital goods, and the organization and supervision of the labor process, including its effect on labor “discipline” and labor productivity. Circuit three involves an analysis of the level and composition of, aggregate demand; it therefore requires a theory of the distribution of income among competing economic classes. Most of these issues and concerns receive scant attention from Keynes and Minsky. One might even argue that Marxists have been better Keynesians than Keynes because, in their circuits-of-capital analysis, they have tried to deal seriously with those real-sector

determinants of the marginal efficiency of capital that Keynes defined to be important but never emphasized in his own work.

The reader who is not familiar with Marxian theory might assume that the first two circuits of capital are roughly analogous to the neoclassical concepts of factor markets and the capitalist enterprise, while circuit three is analogous to the output or product market of standard theory. However, this analogy is at best very loose because the perspectives and logical structures of Marxian and neoclassical theory are quite distinct. For example, the economic agents of Marxian theory are not limited to atomistic individuals; economic classes-sets of individuals assigned to similar positions by the social relations of the mode of production- have a role to play as well. Furthermore, in Marxian theory, the economic (and political) “power” of groups and classes influences economic outcomes. Consider, for instance, the way in which the size of the “reserve army” of the unemployed affects real wage determination.

Or, compare the theory of the firm in the two paradigms. The conceptual distinction between labor-power and labor (that is, the distinction between the contractual employment of a worker for some amount of time and the actual productive work or labor-efficiency-units obtained by the firm from that worker) opens the Marxian theory of the enterprise to a much wider set of considerations than fit comfortably in the traditional Walrasian theory of the firm, a theory in which it makes no difference whether workers depend on employment in capitalist enterprises for their survival or if worker-owned enterprises rent capital goods. The efficiency of the enterprise in Marxian theory depends on the effectiveness of the labor control process and the labor discipline it produces; it thus depends on the relative power of capital and labor. This power balance is influenced not only by the condition of the reserve army, but by a broad set of cultural and political forces as well. And technical change must be seen as influenced to some degree by the efforts of enterprise managers to increase their control over the labor process. As a final example of paradigm differences, consider the fact that there is no concept of full-employment equilibrium in Marxian theory; there is always some reserve army of unemployed in existence except at the peak of unsustainable cyclical expansions. Therefore, most of the conclusions of neoclassical general equilibrium theory do not hold in the Marxian world.

Two general characteristics of Marxian theory deserve mention before we move on. First, Marxists have always stressed the contradictory nature of the capitalist growth process. In Marxian theory, capital accumulation depends on the rate of profit, while the rate of profit is determined by conditions in the various circuits of capital which, in turn, are influenced by the rate of capital accumulation. Economic expansion, whether cyclical or secular, undermines the conditions in the

circuits that are required for its continuation; busts inevitably follow booms and eras of prosperity bring secular crises in their wake because growth eventually erodes the foundations supporting a high profit rate. Indeed, there is a special-field of Marxian analysis-crisis theory-that analyzes the systemic forces in the capitalist accumulation process that tend to lower the rate of profit and eventually transform growth into collapse.

A number of real-sector impediments to sustained accumulation have traditionally been stressed in the crisis theory literature. I will briefly mention three of them.⁹ First, an economic expansion may cause a substantial decline in the reserve army of unemployed. In this circumstance workers can successfully struggle *for* higher wages, while increased labor militancy reduces labor discipline in the workplace. When real-wage gains outstrip productivity growth the profit share falls, the profit rate declines, and the pace of accumulation falters. Second, if the character of accumulation is such that the rate of unemployment remains high (or if other economic, political, or social conditions keep labor relatively weak), then the profit share may be too high to permit a balanced growth between the supply and demand for capital goods and consumer goods. In this case a disproportionality problem-here an “underconsumptionist” crisis-can create excess effective aggregate supply and a decline in the realized rate of profit. Third, some Marxists argue that the class relations of capitalism lead to a labor-saving bias in technical change that raises the capital/labor ratio and creates a tendency for the rate of profit to be dragged down over time. To flesh out the dynamics of instability, of course, these real-sector profitability problems must be embedded in the dynamics of financial markets.

The second characteristic of Marxian theory worth noting is that it stresses the existence of significant economic and political conflicts of interest among agents occupying different positions in the structure of the economy. No doubt Marxists have often used the idea of class struggle as an excuse for failing to come to grips with the complex character of politics and culture in modern capitalist society. Nevertheless, the idea that groups of people who have fundamentally different roles to play in the economic system will hold economic objectives that are sometimes in conflict with each other, will often see their society from different perspectives and through different paradigms, and will struggle over economic and political issues is crucial to understanding the economic and political events of this era or any other era. The centrality of the concept of class

⁹ See Weisskopf (1979) for a concise summary of some of the theoretical and empirical debates in the Marxian crisis theory literature.

conflict in the Marxian tradition and its absence from the Minsky-Keynes tradition is one of the most significant differences between them; this is perhaps most obvious when comparing the way the traditions analyze the economic role of the government.

Minsky and Keynes on Secular Crises and the, Economic Role of the Government

Minsky's endogenous instability thesis also has a secular or trend aspect. Financial fragility and the complex web of financial intermediation associated with it can build up across business cycles, especially if the central bank is in a position to act as lender of last resort in cyclical downturns. In this case, each recession will be counteracted before the debt deflation process or the price deflation process has had a chance to proceed very far. As a result, each cycle will be financially more fragile than the last, and the underlying rate of inflation will rise from one cycle to the next. The end result of this process is stagflation: weak economic expansions aborted by high interest rates, credit crunches, accelerating inflation, and balance-of-payments crises which are followed by recessions that are cushioned by monetary policy when they threaten to trigger a wave of important bankruptcies.

Minsky notes in his essay: "What is done to break inflation leads to what is diagnosed as at least an incipient financial crisis, and what is done to abort the threatened financial crisis leads to inflation." Traditional macropolicy institutions, in Minsky's view, are incapable of resolving the contradictions of stagflation; they are both unwilling to accept the deep depression required to eliminate financial fragility and unable to arrange long-term growth in a financially fragile environment. Therefore, he concludes that some new set of policy institutions is a precondition for ending the secular crisis of the 1970s and 1980s.

The main problem, in Minsky's view, is that "government interventions that now rule are mainly concerned with maintaining consumption, there is no significant government involvement in resource creation aside from defense." A large government that cannot directly influence resource creation (that is, investment) cannot be an adequate vehicle for resolving the economic problems of the day. Further, it cannot be true Keynesian government. "When Keynes advocated a larger role for the state he recommended a 'somewhat comprehensive socialization of investment,' that is, that the creation of resources be separated from the narrow profit calculus and be undertaken and stabilized with social purposes in mind." Minsky carries the thrust of Keynes's policy forward by arguing that "American capitalism cannot be progressive unless there is some comprehensive socialization of several facets of investment activity." Although unclear as to the precise nature of the institutions or policies associated with a more powerful role for the state, Minsky is clear about the necessity for a new policy revolution: "Policy needs to enter upon the as yet uncharted course in

which the rules for a somewhat comprehensive ‘socialization of investment’ and the containment of liability structures are being examined.”

Are Minsky’s proposals for a qualitatively more powerful Keynesian state consistent with Keynes’s writings on the appropriate economic role of the government? Most economists would answer that question in the negative. After all, Minsky’s endogenously unstable economy, subject as it is to cyclical and secular crises, and his argument in support of the necessity of governmental control of the investment process and restrictions on the liability structures of enterprises bear little resemblance to mainstream American Keynesian macroeconomic theory and policy. In other words, they certainly cannot be found in Samuelson’s textbook. In my opinion, however, Minsky’s work makes him one of the few true Keynesians in the profession today. For, contrary to what most American economists believe about Keynes’s thinking on theory and policy, his critique of capitalism was quite radical and his policy proposals were more far-reaching and revolutionary than mainstream Keynesians have ever recognized. A brief review of some of Keynes’s major conclusions concerning government economic policy will help in evaluating the extent to which Minsky is faithfully bringing Keynes’s analyses and insights to bear on the current crisis of the capitalist economies. (See Crotty, 1983, for a more extensive treatment of this issue.)

In the early 1930s, Keynes argued that the two major threats facing the contemporary world—depression and the possibility of world war—were in large part derivatives of existing capitalist institutions. He was straightforward and aggressive in his indictment of capitalism: “The decadent international but individualistic capitalism, in the hands of which we found ourselves after the war, is not a success. It is not intelligent, it is not beautiful, it is not just, it is not virtuous—and it doesn’t deliver the goods. In short, we dislike it and are beginning to despise it” (1933: 760-61).

The achievement of the dual objectives of peace and prosperity, Keynes believed, required the creation of new, more powerful government institutions charged with controlling the outcomes of economic activity. In essence, Keynes proposed that Britain begin an evolutionary, trial-and-error process of creating a more planned and controlled economic system at home while it simultaneously instituted a system of government controls over the international movement of goods and especially money. The international controls were a necessary condition for the achievement of domestic economic objectives. What was needed, he argued, was “a transition toward greater national self-sufficiency and a planned domestic economy” (1933: 767).

To promote full employment and domestic prosperity, the state, Keynes believed, would have to take responsibility for basic economic decisions concerning the level of investment and saving, the allocation of investment among competing uses (broadly defined), and the general

distribution of income. State control of the investment process through public works, public or semipublic corporations, investment planning boards, credit allocation schemes, and so forth-not monetary and fiscal policy as conventionally defined-was the corner-stone of Keynes's domestic economic policy proposals. In "The End of Laissez-Faire" (1926) he had written: "I believe that some coordinated act of intelligent judgment is required as to the scale on which these savings should go abroad in the form of foreign investments, and whether the present organization of the investment market distributes savings along the most nationally productive channels" (1963: 318).

Because his theory of capitalist instability was based on the instability of private investment spending, Keynes made public investment the cornerstone of his full-employment program. In *The General Theory* (1936) he proposed "a somewhat comprehensive socialization of investment" (1964: 378) and spoke of the state "taking an ever greater responsibility for directly organizing investment" (p. 164). Keynes's emphasis on the use of state control of investment to stabilize the economy at full employment continued undiminished in the 1940s. In 1943, he wrote 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" (1980b: 326). That same year, he argued that if, "something like two-thirds or three-quarters of total investment will be under public or semi-public auspices, the amount of capital expenditures contemplated by the authorities will be the essential balancing factor. ...It has nothing whatever to do with deficit financing" (1980b: 352).

Keynes left no precise definition of what he meant by the socialization of investment or state control of the investment process, although in several essays he stressed the key role to be played by "semi-socialized" public corporations run by technical experts, corporations which were to be insulated to some degree from the direct control of elected officials. For example, in "The End of Laissez-Faire" he argued that "progress lies in the growth and the recognition of semiautonomous bodies within the state-bodies whose criterion of action within their own field is solely the public good as they understand it-bodies which in the ordinary course of affairs are mainly autonomous within their prescribed limitations, but are subject in the last resort to the sovereignty of the democracy expressed through Parliament" (1963: 313-14). (I return to the political philosophy underlying Keynes's concern with semiautonomy below.)

Although Keynes focused his proposals for full-employment planning on control of investment by public authorities, he clearly understood that the government could not maintain investment at a full-employment level if capital were free to enter and leave the country at will or if trade were to remain completely unregulated. From the early 1930s until his death in 1946, Keynes

consistently argued in support of strict capital and foreign trade controls as an essential part of full-employment planning. For example, in 1941 he wrote, “I share the view that central control of capital movement, both inward and outward, should be a permanent feature of the post-war system” (1980a: 52). A year later he argued that “the whole management of the domestic economy depends upon being free to have the appropriate rate of interest without reference to the rates prevailing elsewhere in the world. Capital control is a corollary to this” (1980a: 148-49).

Given my reading of Keynes, I would have to conclude that Minsky’s analysis of the current crisis and his call for radically increased government authority to control economic activity as a precondition for ending the crisis constitute perfectly sound Keynesian economics. At this point, however, I would, like to shift the focus of discussion from Keynes to Marx and raise two questions about Minsky’s work on secular crises. First, how might the strengths and weaknesses of Minsky’s theory be assessed from a Marxist perspective? Second, what are the differences between Marxian and Minskyan-Keynesian views on the nature of government economic authority and on prospects for the kind of radical change in that authority that both Keynes and Minsky have proposed? To answer these questions I must examine, however briefly, Marxian perspectives on the question of long-term crises in the capitalist economy.

Marxian Theoretical Perspectives on Secular Instability

An analysis of a specific historical long-term economic and social crisis cannot be conducted exclusively at the very abstract theoretical level of the circuits of capital analysis. Over the past decade or so, there have been a number of efforts by economists working in the Marxist tradition to make concrete the circuits of capital analysis in order to bring its insights to bear on the long-term economic problems of the current era. The initial step involved in this project is the recognition that each of the circuits of capital has a specific *institutional* foundation. There is no such thing as “*the* labor market,” for example; rather, there are specific organizations, institutions, traditions, and practices involved in making labor of various kinds and skills available to different enterprises in different places and circumstances. The same thing can be said of “markets” in general or of the concept of “the capitalist enterprise” itself. For purposes of very abstract theory, it may be sufficient to represent the firm as a black box that somehow transforms inputs into outputs. However, to understand a historically specific economy, we need to know something about the way the typical enterprise is organized and structured, what its internal division of labor is like, how its workers are motivated and controlled, and so forth. A good example of this need for institutional concretization is the intense interest currently being shown in the relative merits of the organizational structure of manufacturing enterprises in Japan and America.

Conversely, the circuits-of-capital framework can be used to organize the large number of individual institutions associated with the accumulation process into a coherent structure; organizing institutions in terms of their relationship to the circuits of capital provides a conceptual articulation of individual institutions or a structure of institutional relations. David Gordon has coined the term “social structure of accumulation” (*SSA*) to capture the unique articulation of institutions that characterizes a specific historical era.

The recognition of the need for institutionally concrete historical analysis in combination with some general themes drawn from the study of the history of capitalist economies has created the basic material used in some of the more interesting analyses of the current crisis. The following hypotheses about that economic history are of special significance. First, the basic institutional structure of the capitalist economy changes rather dramatically over time. The character of labor markets, the structure of the enterprise, the economic role of the state, the international financial system, etc., are profoundly different today from what they were fifty or a hundred years ago. Second, and more controversial, there appear to be eras in which the accumulation process, on average, functions rather effectively sandwiched between periods of greater economic and social instability. Third, the first two hypotheses taken together suggest that each new era of growth and stability involves a basic institutional structure that is qualitatively different from the *SSA* of the era of prosperity that preceded it.

Efforts to integrate the concretization of Marxian crisis theory with these hypotheses about the history of growth and instability into a theoretical structure capable of dealing with the turbulence of the 1970s and 1980s have not yet developed into a completely satisfactory “theory” of structural crises. However, there are a number of important ideas that unify work in this area. (For a sample presentation of *SSA* ideas, see Gordon, Edwards, and Reich, 1982: chap. 2.) When combined with some of the specific facts of the current period, these ideas generate at least an outline of an understanding of the ongoing crisis of our era. The following hypotheses are held in common by a number of authors, not all of whom use a formal concept equivalent to the *SSA* in their writings.

1. Each broad era of growth, or stage of development, of the capitalist economy is characterized by a core set of economic (and noneconomic) institutions—a social structure of accumulation—that distinguishes it from the previous stage of growth.

2. Through this characteristic institutional structure of a high-growth era, the circuits of capital (or economic relations) are organized so that all of the potential impediments to a high-trend profit rate and to sustained capital accumulation identified by Marxian crisis theory are prevented

from reaching serious enough proportions to threaten secular growth. (Of course, business cycles take place both in eras of prosperity and in eras of stagnation.)

3. As economic growth takes place over long periods of time, the social relations and therefore the institutions of the SSA change and can no longer support growth, and/or the institutional requirements for successful capital accumulation change and the old SSA is no longer adequate to the task. At some point in each growth era then, the trend profit rate declines and a secular crisis of instability, turbulence, and uncertainty erupts, replacing the confident prosperity of the preceding stage. (For example, the secular decline in the profit rate that set in after 1965-66 is typically seen as initiating a chain of events leading to the crisis of the 1970s and 1980s.)

When stated so succinctly, this idea may seem mechanistic -- as if institutions changed themselves. However, the intent is to capture the effect on institutions of the actions of human subjects. Economic agents, as individuals and as members of groups, pursue their perceived self-interest within the institutional structures of the society which define and organize them. Over time, the actions of these individuals result in the alteration and reconstitution of these structures.

4. A secular crisis of accumulation, along with the political and social turbulence it engenders, cannot end unless major institutional or structural change occurs, that is, unless a new and qualitatively distinct social structure of accumulation is put in place. To put it more concretely, the prosperity of the 1950s and 1960s cannot be recreated in the 1980s on the institutional foundation of the earlier period. A new era of relatively smooth accumulation requires fundamental institutional change in one or more major areas of the SSA.

5. The particular form that the new SSA will take is not dictated by technical economic conditions alone. Rather, the new SSA evolves out of political debate and domestic and international economic and political struggle. For example, it is no accident that this century's two major periods of crisis in the world economy ended in world wars. Economic conditions shape and influence the outcome of this conflict and delimit the feasibility of various potential institutional adaptations, to be sure; but they do not predetermine the outcome of social conflict.

Marxian Explanations of the Current Crisis

What kind of explanations of the economic difficulties of the 1970s and 1980s have Marxists constructed using this theoretical framework? How do these explanations differ from the one presented by Minsky? I cannot survey the emerging Marxist literature here, but even a sketch of some of the main ideas associated with it should be sufficient to highlight two fundamental differences between the, Marxian and Minsky-Keynes tradition. (For an example of the genre, see,

Bowles, Gordon, and Weisskopf, 1983.) First, Marxian explanations of the crisis are broader in scope because Marxian theory emphasizes many different potential impediments to accumulation. These explanations focus attention on some of the nonfinancial institutions and variables neglected by Minsky. Second, discussions of the changing economic role of the government and the evolution of economic policy are treated quite differently in the Marxian and Keynesian traditions. Just as class conflict is an important concept in Marxian theories of the economy, economic and political conflicts of interest and struggles among different classes or interest groups play a central role in Marxian writings on the economic role of the government and the formation of economic policy.

The general flavor of Marxian writings on the current crisis is suggested by the set of guiding ideas listed above. The interwar years in Europe and the decade of the 1930s in the United States were periods of crisis and instability that ended only when the conflicts and struggles of the 1930s and 1940s culminated in the development of a new and qualitatively different social structure of accumulation in the domestic and in the international economy. We are all familiar with its most important elements: the Keynesian welfare/warfare state; a new international financial system based on the Bretton Woods Agreements and the dominance of the U.S. dollar; a stable international economic, political, and military order reflecting the geopolitical hegemony of the United States; relatively harmonious capital-labor relations in the core of the economy resulting from the de-radicalization and legitimization of the industrial unions that arose out of the labor conflict of the 1930s; and the reconstruction of a robust domestic financial environment.

The general explanation of the outbreak of economic instability in the late 1960s and the early 1970s, put quite simply, is that the process of growth during the preceding twenty years led both to fundamental changes in key areas of the SSA and to the inability of sections of the postwar SSA to perform their circuits-of-capital functions. As a result, the trend rate of profit declined and crisis broke out. A period of economic and political struggle began over who would bear the burdens of the crisis and how the crisis would be resolved, a period that has yet to end. The spirit of this discussion and debate can be picked up by considering the following examples of changes that occurred in the key elements of the postwar SSA.

First, the liquid and robust domestic financial environment of the early postwar period was qualitatively transformed by the growth process of the era. The 1960s and 1970s saw a spectacular increase in the complexity and importance of financial intermediation. Financial fragility or oversensitivity replaced financial health, and credit crunches and debt crises became the order of the day. I mention this development first because the description and analysis of this process is

Minsky's major contribution to our understanding of the current crisis, a contribution that fits quite naturally into the SSA analytical framework.

Second, in the 1950s and 1960s the system of labor relations in the core of the economy was quite consistent with the requirements of accumulation. Real wage gains were high, yet they were generally no greater than trend productivity gains. As a result, satisfactory profits were achievable in a relatively noninflationary environment. The optimism and confidence brought on by the low unemployment rates of the 1960s, however, fostered increased worker militancy, which in turn led to real wage gains in excess of productivity gains. This development, in concert with other important events taking place in the same period, helped create profit, inflation, and balance-of-payments problems by the late 1960s. With the existing framework of capital-labor relations no longer seen as consistent with high profits, businesses unleashed an economic and political assault on the labor movement and on traditional labor relations practices. This attack has been increasingly successful, especially since the blatantly antilabor Reagan administration has been in power.

Third, the Keynesian welfare/warfare state of the 1950s and 1960s helped create a domestic economic environment within which capital accumulation flourished. However, popular political struggles, especially in the latter part of the period, led to an expansion of the domestic economic role of the government. As a result, social welfare spending grew far beyond a level thought by the business community to be consistent with high profits; a conservative backlash against social programs ensued. Moreover, expansionary government economic policy in the early and mid-1970s, although it may have helped prevent an economic collapse of Great Depression proportions, made an important contribution to the accelerating inflation of the decade. Thus by the late 1970s, the traditional Keynesian economic role of the government was increasingly portrayed as an impediment to, rather than an essential condition for, growth and stability. Reaganism and Thatcherism are reflections of the perceived inability of the traditional Keynesian state to restore long-term prosperity.

Fourth, the international monetary and financial order created after World War II provided a stable and predictable environment within which international trade and investment could flourish. This environment contributed to the prosperity shared by most of the advanced industrial countries in the early postwar period. However, changing economic conditions over the period, along with pursuit of self-interest by the major countries involved in the international economy, led to rising pressures upon the Bretton Woods Arrangements, pressures that eventually brought about its collapse in the early 1970s. The past decade has seen the creation of an ocean of rootless

international liquidity. As a result, the world economy has experienced unpredictable exchange-rate gyrations that inhibit international trade and investment, as well as intermittently threaten-as they did in 1979-to destabilize totally international financial markets. Finally, there has been the potentially disastrous buildup of severe debt burdens in many of the developing countries.

Fifth, in the 1950s the United States was so economically and militarily dominant that it could impose a stable political and economic order on world affairs. Indeed, the early postwar period has often been referred to as *Pax Americana*. Although America remains the strongest power in the world, the relative stability of *Pax Americana* has turned into economic and geopolitical turbulence. Over the course of the past few decades, Europe and Japan have become serious competitors with the United States for international markets and sources of raw materials. Meanwhile, the Soviet Union has gained in military strength, and many third world countries have rebelled against neocolonialism. Vietnam was the most important of these rebellions. This confluence of events- increasing competition in output markets, rising raw materials costs, and escalating geopolitical instability-adversely affected the profit rate attained by U.S. corporations. Without the creation of some new set of relatively stable international economic and geopolitical arrangements, it is hard to envision a repeat of the prosperity of the 1950s and 1960s. On the other hand, it is rather easy to imagine any number of scenarios involving the outbreak or intensification of wars in various centers of instability and conflict that could ultimately engage the superpowers.

Each of these examples could be discussed at great length and several others could have been mentioned-for instance, the multinationalization of the large enterprise with all of its important ramifications. These five will suffice, however, to provide a sense of the broad character of some of the discussions of the current economic situation in the Marxist literature and to make the following arguments.

First, an adequate analysis of the causes of our current economic malaise must evaluate the main determinants of profitability and capital accumulation in the *real* sector as suggested in the circuits of capital framework and must deal with the international economy. Financial fragility and international debt burdens are only a part of the explanation of the current crisis. Second, the analysis must go beyond a discussion of why economic variables such as interest rates, deficits, and wages keep getting out of line to consider the status of the institutions that organize economic activity. The first of these levels of analysis is adequate for understanding business-cycle problems; a secular or long-term crisis must be studied at the second and deeper level. Third, an adequate analysis must recognize that fundamental institutional change is a prerequisite for resolving a secular crisis. It should also recognize that economic and political struggle or conflicts among

competing economic interest groups or classes is an essential part of the process through which institutional change takes place. Nowhere is this last point more evident than in the comparison of different analyses of the changing economic role of the government.

Marx versus Keynes-Minsky on the Economic Role of the Government

Political economy is a social science; its practitioners cannot predict the outcome of political and economic struggles the way natural scientists can predict the appearance of comets. Nevertheless, some theoretical frameworks are more helpful than others in conceptualizing and describing the process through which economic and political institutions and practices change over time. I would like to examine the case of the changing economic role of the government and use it to support the proposition that the Marxist tradition is more helpful in understanding these changes than is the tradition represented by Minsky-Keynes because of the central role the former gives to political conflict among economically defined interest groups.

I have argued that Keynes had a far more radical view of the appropriate role of the government than has traditionally been assumed; he wanted public authorities to control directly the bulk of investment activity, and he wanted the central government to control international trade and capital movements. But he did nothing to help us understand the political process through which these radical structural changes-this movement to a new SSA -could or would be brought about. The problem is not that Keynes had no strong political beliefs or ideological presuppositions. On the contrary, his political essays suggest that he was profoundly affected by the revolutionary upheavals that took place during and after the First World War. His greatest fear was that the wars and depressions of the period would lead to a class-conscious political movement of workers in England, a movement that would reconstitute the social structure of accumulation along radical socialist lines.

Keynes himself was quite class conscious and knew the class to which he owed allegiance. "I can be influenced by what seems to me to be justice and good sense," he once argued, "but the class war will find me on the side of the educated bourgeoisie." It was this fear of a radical working-class political movement that explains his interest in "semiautonomy" for the public authorities that were to direct investment and control capital flows in his new SSA. They were to operate under the guidance of an elite corps of upper-class intellectuals (such as himself) and were to be insulated to a significant degree from oversight by elected officials.

Yet in spite of the fact that economic classes and potential class conflict strongly colored his political views, Keynes provided no conceptual space for these concepts in his theoretical

apparatus. In the works with which most of us are familiar, Keynes wrote as if he assumed that any institutional change that he believed to be in the “national” interest would somehow-through some unspecified process- be forthcoming no matter what class-based forces stood against it. Presumably he really believed the thought with which he ended *The General Theory*: “soon or late, it is ideas, not vested interests, which are dangerous for good or evil.” Whatever he believed, his theoretical framework cannot aid us in our own attempts to understand the ongoing political conflicts of the current era.

Minsky’s discussion of the appropriate economic role of the government is quite similar to Keynes’s. He also proposes radically new government machinery to control or guide the economy. In recent writings he has supported not only publicly controlled investment, and government restrictions on corporate liability structures, but also unspecified government institutional or policy changes that would make full employment, price stability, and international payments equilibrium mutually compatible. Unfortunately Minsky is, if anything, less forthcoming than was Keynes about the problems and prospects involved in trying to bring about such radical change.

In the Marxist tradition, on the other hand, economic institutions and political processes are part of an integrated theoretical analysis; economics and politics are mutually interactive. This makes it necessary for those influenced by this tradition to confront questions concerning the process through which changes in government institutions and policies evolve. In this tradition the political process is assumed to involve conflicts of interest substantially, though not exclusively, derived from the competing economic interests of the conflicting parties and the different ideological presuppositions associated with their class differences. Put somewhat differently, Marxian analysis requires that questions of vested interests, conflicts of interest, and the political power of competing economic groups be interjected in discussions of the changing economic role of the government.

I want to examine briefly two examples of changes in government economic programs and policies, to illustrate the differences between the two traditions outlined here: Reaganomics, and the debate over industrial policy. Most economists have analyzed the economic policies of the Reagan administration using the concepts of supply-side economics and monetarism and have contrasted his policies with traditional Keynesianism. Many economists have even worried about the distributive equity of Reaganomics. But few have written as if they were aware that Reagan’s programs represent the political victory of one set of economic agents over others, that his administration has dramatically shifted the economic burdens of the current crisis from capital to labor, from the rich to the welfare poor, the working poor, and the lower middle class, from the

propertied, professional, and managerial strata to the rest of society. One is tempted to argue that only a traditionally trained economist could fail to see the economic policies of the present era in class terms and in conflict terms.

Consider some of the Reagan administration's programs: massive tax cuts for wealth-holders, corporations, and upper-income recipients; drastic cuts in social welfare programs; attacks on the rights and powers of trade unions and of individual workers (for example, the gutting of OSHA, the transformation of the NLRB into a decidedly pro-management body, and the vicious treatment of the PATCO workers); support of virtually uncontrolled corporate power through deregulation, the weakening of the SEC, and a change in antitrust philosophy; and the weakening of consumer and environmental protection. What is this program if not the political victory of one segment of our economy over others?

Even Reagan's macropolicy must be viewed in class terms if it is to be properly understood. The sustained high levels of unemployment and the holes cut in the social safety net have combined to weaken workers substantially in their struggles with their employers. The take-away contracts, declining union influence over the organization of the labor process, and increasing success of union busting of the recent past could not have taken place under conditions of full employment and reasonable job security. It is hardly surprising, then, that Reagan has near unanimous support among corporate executives while the AFL-CIO is trying desperately to bring about his defeat.

I do not mean to imply that monetarism and supply-side economics are merely advertising slogans cynically used by Reagan and his powerful supporters to help market their self-aggrandizing economic programs. To some extent they are honest reflections of the way these people think about the economy. In this sense, these economic theories represent the "truth" about what the Reagan administration is trying to accomplish through its economic policies. But they do not represent the whole truth and nothing but the truth. Taken as economic doctrine by themselves, they hide the fact that the political forces that support Reagan and those that oppose him represent competing economic interest groups, and that Reagan's economic Darwinism brings immediate gains to his friends and immediate and often terrible costs to those who are not his friends.

The point is that one cannot possibly understand the recent past or intelligently speculate about the future developments in government economic policy using a theory that totally separates the way in which the structure of the economy organizes people into competing interest groups from its analysis of the political process. The "radical politics" of the Reagan administration constitute a distinct rupture with the economic policies, programs, and guiding ideology of postwar presidents. That this rupture took place at the end of the 1970s is not an accident; Reaganomics is a

political product of the secular economic crisis of the past decade. It must be thought of as an intermediate stage in the struggle over the reconstitution of the new SSA. My own understanding of the nature of the crisis of the 1970s and 1980s leads me to believe that Reagan's free-market economic Darwinism is not the wave of the future. I would guess that the government in the future SSA that ultimately replaces the Keynesian government of the postwar SSA will have far greater authority to organize and direct economic activity, greater planning responsibilities, and a larger role for industrial policy than it currently exercises.¹⁰ But whatever the future brings in this regard, we will not understand how and why history produced its outcome unless the theory used to investigate the issue incorporates political aspects of class-based conflicts.

My second example is the debate over reindustrialization or "industrial policy" that has been taking place off and on for about a decade, ever since the economic collapse in 1974-75 convinced many that we had entered a new era in which the old ways of organizing the economy were incapable of producing sustained prosperity. It is a debate over the appropriate economic role of the government, a debate that increases in intensity during exceptionally difficult periods such as 1974-75, the last part of the Carter administration, or the deep recession of 1980-82 and fades out during cyclical upturns. The proponents of reindustrialization have argued that in the new economic conditions of the 1970s and 1980s, including intense international competition, frequent geopolitical and economic shocks, the rise of sunshine industries, and the fall of smokestack industries, the government will have to take a far more active role in guiding and managing the economy than it did in the glory days of the 1950s and 1960s. Proposals put forth by supporters of this general view include a new Reconstruction Finance Corporation to finance investment projects with public funds; government-organized industry or regional tripartite planning bodies with representatives of capital, labor, and government (New York's Municipal Assistance Corporation, or Big MAC, is often mentioned as an example); a Japanese model of government-industry cooperation; the relatively strong government planning functions of the original Hawkins Bill in the House of Representatives (the bill that eventually became the relatively harmless Humphrey-Hawkins Act); a public energy corporation; and several variants of a new social contract with an incomes policy and wage-price controls.

¹⁰ My judgment that the government will become more powerful (though perhaps smaller) in the foreseeable future is shared by Robert Heilbroner, among others. Last year he wrote that "despite all the efforts of Reagan and Thatcher to the contrary I cannot see the future of capitalism without the national governments playing a still more prominent role in its propulsion, support and guidance" (*The New Yorker*, August 29, 1983, p. 77).

Reindustrialization programs have been proposed by individuals and organizations representing very diverse political constituencies and different economic interests. Proponents of some form of industrial policy can be found among traditional liberal politicians such as Ted Kennedy, neoliberals such as senators Gary Hart and Paul Tsongas, labor organizations such as the AFL-CIO, maverick academics such as economist Lester Thurow or lawyer Robert Reich, left-wing economists such as Samuel Bowles, David Gordon, and Thomas Weisskopf, and influential businessmen such as the investment banker Felix Rohatyn. Each of these programs proposes a redistribution of power over economic processes and outcomes, and each involves a different distribution. Nevertheless, most of these programs have been put forth as if they were in some “national interest” shared in common among all economic groups; support for or opposition to each plan is assumed to depend on neutral economic efficiency criteria. Similarly, few proponents of reindustrialization programs discuss the political coalitions and campaigns that might be put together to get these programs into operation, and few discuss the vested interests that will have to be overcome if the programs are to be adopted and implemented.

Indeed, the whole discussion reminds me of the proposals for new and more powerful government institutions and policies put forth by Minsky and Keynes. Radical new directions for government economic policy are put forth in both instances, yet they are presented in a class-blind, idealist political vacuum. It is as if no one knows about or cares to remember the fact that relatively ambitious, progressive proposals for government economic planning functions were put forth first, in 1945, in the form of the Full Employment Bill and later, in 1975, in the form of the Hawkins Bill. These attempts to affect two succeeding social structures of accumulation were both supported by alliances of liberal politicians and labor groups and were both opposed by coalitions of conservative politicians and business interests. The conservative business groups were basically victorious in both cases; they were able to substitute much weaker legislation for the original bills (the Taft-Whittington Employment Act of 1946 in the first case and the Humphrey-Hawkins Act in the second), legislation which left the existing structure of economic power substantially intact.

These two examples of unsuccessful struggles to alter substantially the economic role of the government illustrate the problem with both the Minsky-Keynes proposals and the current debate over industrial policy. These proposals are presented and this debate is largely conducted as if politics and economics were two separate spheres of human activity totally isolated from and independent of one another and as if the political process were devoid of conflicts of interest originating in the structure of the economy. Whatever other faults it may have, the Marxist-influenced debate on the current crisis and on the resulting short-run political battles focuses

attention on the class-based political conflicts that will play an important, if not dominant, role in determining the new economic role of the government that will evolve from this process. And it further suggests that those people who would like to see the government play a more progressive and egalitarian role in the economy must be prepared for the political struggle it will take to achieve this objective. The economic historians who will have to explain to future generations why it was that the SSA of the immediate post-World War II period gave way after a long period of turmoil to the particular SSA of the 1990s will need Keynes and Minsky to guide their work, but they will need Karl Marx as well. Marx will help them understand that they need to look at a broader set of issues than Keynes and Minsky. Marx will also help them understand why, given the technological feasibility of so many radically different kinds of government programs and policies, the particular economic role of the government in the new SSA came into being. As I see it, Marx, Keynes, and Minsky might all be embarrassed to be found in bed together, but they are not such strange bedfellows after all. Each has his role to play in constructing a theory of political economy adequate to our needs.

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