

COULD KEYNESIAN POLICIES END THE SLUMP?

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The proximate cause of crises

- For Marx, the proximate cause of crises is the fall in the average rate of profit (ARP). Recent studies have shown that this thesis not only is logically consistent but is also supported by a robust and growing empirical material. Due to lack of time, I shall have to assume that this is the case.
- If falling profitability is the cause of the slump, the slump will end only if the economy's profitability sets off on a path of sustained growth.

Then, the relevant question for many Marxists is

- Can Keynesian policies restore the economy's profitability? Can they end the slump?

What are Keynesian policies?

- **First**, they are *state induced* economic policies.
- **Second**, they can be *redistribution* policies or *investments* policies.
- **Third**, they should be *capital financed* and not *labour financed*. If labour-financed, they are neo-liberal policies.
- **Fourth**, in case of state induced investment policies, they can be either *civilian* (mainly in public works like highways, schools, hospitals, etc., in order to avoid competition with those private sectors already experiencing economic difficulties) or *military*.

- I shall not deal with 'Military Keynesianism' because presently this is not what Keynesian economists propose to end the crisis. Some might think that a major war might be the only way out of the depression. This is an open admission of the monstrosity of this system. But then, why save it?
- Then, what follows refers only to civilian Keynesian policies. Let us consider redistribution first.

- Supposedly, the sale of unsold consumption goods would spur the production of means of consumption. This would generate the demand for means of production. An upwards cycle would start. And this is why these policies are supposed to be pro-capital as well. Both capital and labour would gain.
- This is the basis of Keynesian reformism, of class collaboration.

State induced *redistribution* policies.

- Suppose the state brings about a redistribution of value from capital to labour through pro-labour legislation, progressive taxation, etc. Wages (direct, indirect, and deferred) rise. More consumption goods are sold and labour consumes more. This is why these policies are supposed to be pro-labour.

- But does labour's greater consumption really cause a greater production of consumption goods and thus greater employment and economic growth?
- Suppose first that some consumption goods are unsold. This is the hypothesis behind Keynesian interventionism. In this case, higher wages cause the *sale* of unsold consumption goods and not a greater *production* of these goods.
- *Keynesian redistribution fails in its own terms*, in terms of production and thus employment and recovery.

- But capitalism prospers not if production rises but if profitability rises. Let us then introduce profitability. If a capitalist cannot sell her output, she suffers a loss. If later, due to higher wages, those commodities are sold, she realizes that unrealized profit. Profit and loss cancel out. But profitability falls.

- Let us see why. Take first the sector producing means of consumption. On the one hand, it suffers a loss due to higher wages but on the other it can sell unsold means of consumption for an equal price. The numerator of the rate of profit is unchanged. However, the denominator rises due to the higher investment in variable capital. Its rate of profit falls.

Means of consumption

- $60MP+40LP+40P$
- $RP = 40/100 = 40\%$
- $60MP+(40+4)LP+(40+4-4)P$
- $+4$ = higher investment in labour power
- $+4$ = extra profits due to higher sales
- -4 = loss due to higher wages
- $60MP+44LP+40P$
- $RP = 40/104 = 38.5\%$
- Labor's consumption increases by 4 but the RP falls from 40% to 38.5 %, i.e. by 1.5 percentage points.

- Take next the sector producing means of production. Higher wages are a loss and also a higher capital invested (in labour power). Its numerator decreases and the denominator rises. Its rate of profit falls. Its rate of profit falls on both accounts.

Means of production

- $80MP+20LP+20P$
- $RP = 20/100 = 20\%$
- $80MP+(20+2)LP+(20-2)P$
- $+2 =$ higher wages
- $-2 =$ loss due to higher wages
- $80MP+22LP+18P$
- $RP = 18/102 = 17.6\%$
- Labour's consumption rises by 2 but the RP falls from 20% to 17.6%, i.e. by 2.4 percentage points

- Finally, the higher wages in sector I (the producer of means of production) are an increased consumption by the labourers in that sector and thus an extra profit for sector II (that produces the means of consumption). But they are also an equal loss for capital in sector I. The loss in sector I and the profit in sector II cancel out. Thus,
- $(60+80)MP+(44+22)LP+(36+18+2-2)P$

- Before wage rise:
 $(80+60)MP+(20+40)LP+(20+40)P$
- $ARP = 60/200 = 30\%$
- After wage rise:
- $(60+80)MP+(44+22)LP+(36+18+2-2)P$
- $ARP = 54/206 = 26.2\%$
- Labour's consumption rise by 6 but the ARP falls from 30% to 26.2%, i.e. by 3.8 percentage points

- *Keynesian redistribution fails on grounds of profitability as well.*

- Suppose now that wages keep rising up to the point where all consumption goods are sold. Would a further rise in wages spur the extra production of consumption goods? No.
- *Production increases both if profitability rises and if there is demand for the extra output, i.e. if the extra surplus value can be realized.*
- Production does *not* rise if one of these two conditions is not satisfied.

- Higher wages increase the demand for consumption goods but at the same time lower profits.
- *If profits fall, capitalists reduce their output in spite of higher demand* both because less surplus value can be generated and reinvested and because, due to higher wages, the weaker capitalists go bankrupt and cease production.
- *Production decreases.*

- Therefore, after an initial rise, if production decreases, consumption might decrease as well.
- However, in what follows, I shall assume the most favourable case for the Keynesian hypothesis, i.e. that labour's consumption increases.

- It follows that the kernel of the Keynesian equation
 - Higher wages = more consumption = more production = end of the slump
 - is wrong because
- (1) in case of remnant sales, production does not rise but profitability falls and
- (2) if all output is sold, higher wages decrease profitability and thus production.

The fallacy of Keynesian redistribution

- *Higher wages increase consumption but decrease profitability.*
- *Thus, they cannot be a counter-cyclical measure, they cannot end the slump.*

- The Keynesian hypothesis *omits profitability* as one of the two essential factors governing production. The political consequences are far reaching. In fact, this omission is essential for the equilibrium hypothesis.
- If a greater demand (induced by higher wages) were matched by greater production, the economy would tend towards the point at which demand and supply meet. This is the equilibrium point. But if greater demand induced by higher wages causes a fall in production through falling profitability, *no point of equilibrium can be reached*. Higher wages contribute to the movement towards the crisis.

- This conclusion is extremely important because, by denying equilibrium, we deny that this system is rational. Bourgeois economics, on the other hand, holds that the system is in or tends towards equilibrium and that therefore it is rational. The consequences for labour's struggle are devastating because the struggle against this system becomes a struggle against a rational system and thus an irrational, spontaneistic struggle. But if the system is irrational because it tends towards crises, labour's struggle become the conscious manifestation of an objective movement.

Pro-capital redistribution

- Alternatively, the state can induce a redistribution of value *from labour to capital* (through falling wages). These are neo-liberal (the opposite of Keynesian) policies. Nevertheless, let us briefly consider them.
- A wage cut increases profitability. But at the same time, it reduces the demand for consumption goods. In this case, capitalists reduce their output not because profits fall but because demand falls.

- Due to falling demand for consumption goods, the extra profits from higher wages are not reinvested in that sector and thus cannot spur investments in the production of means of production. They are either set aside as reserves or invested in the unproductive sectors (commerce, finance, and speculation) where profitability is higher (but only as long as the bubble does not burst). These extra profits cannot get the economy going again.

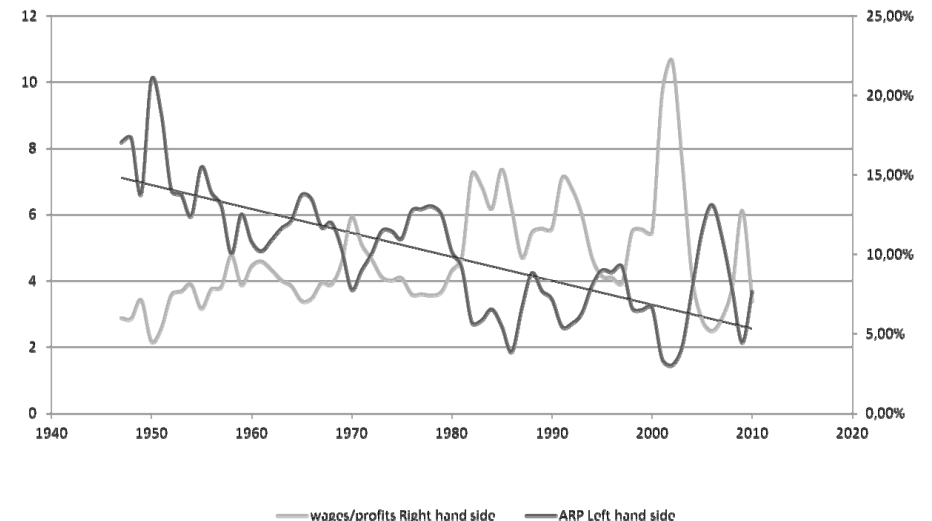
The impotence of redistribution

- In sum, neither pro-labour nor pro-capital redistribution policies can end the slump. This can be empirically substantiated.

Empirical substantiation

- Chart 1 deals with the US productive sectors. It shows that up to 1986, wages rise relative to profits and the ARP falls, conform to Marx but not to Keynesian underconsumptionism. From 1987 to 2009 wages fall relative to profits and the ARP rises, again conform to Marx but not to Keynesian underconsumptionism.
- Both pro-labour and pro-capital redistribution did not prevent the ARP from falling.

Chart 1. The ARP and rate of wages to profits



State induced *investments*

- The strongest case for Keynesian policies is not state induced *redistribution* but state induced civilian *investments*. As a rule, those authors (also Marxists) advocating state induced investment policies as a way to end the slump omit a fundamental point, namely who is supposed to finance these investments. There are two possibilities: *capital financed* and *labour financed* state induced investment policies. I shall consider only capital financed investments because labour financed investments are not what Keynesian authors propose to end the slump.

- Let us distinguish between sector I, the producer of public works, and sector II, the rest of the economy. Surplus value, S , is appropriated (e.g. taxed) by the state from sector II and channeled into sector I for the production of public works. Rather than taxing surplus value, the state can appropriate unused reserves. But as far as capital is concerned, this is a loss and thus a deduction from surplus value.

- Having appropriated S from sector II, the state pays sector I a certain profit, p , and advances the rest, $S-p$, to sector I for the production of public works.
- Consider the effects on the ARP. Sector II loses S but sector I gains p . In sum, private capital loses $S-p$ to the state. The numerator of the ARP decreases by that much. The ARP falls.
- But this is not the end of the story. The capitalized surplus value advanced by the state, $S-p$, is invested by sector I. To determine the effect of this investment on profitability, we must introduce what I shall call the Marxist multiplier.

- $\frac{S-p}{p}$
- sector II $\rightarrow S$ to the State $\rightarrow S$ to sector I
- $\backslash S-p$
- The private sector loses $S-p$. the numerator of the ARP decreases by that much. The ARP falls. Let us introduce the Marxist multiplier.

The Marxist multiplier

- To produce public works, Sector I purchases labour power and means of production from other firms in both sectors. In their turn, these firms purchase means of production and labour power. This multiple effect cascades throughout the economy. Under the most favourable hypothesis for the Keynesian argument, the state induced investments are sufficiently large to first absorb the unsold goods and then stimulate new production. These firms have different organic compositions. At this point, three cases are possible.
 - (a) S-p, the initial investment by sector I, plus the ripple effect throughout the economy are such that they form a representative section of the whole economy. Then, the rate of profit generated by them is equal to the economy's average. The ARP after these investments does not change. The policy fails. This result holds irrespective of the initial investment's organic composition.
 - (b) Alternatively, the chain of investments stops at a point at which the organic composition of all the invested capitals (including the initial ones) is higher than the average. Then, the ARP falls. Again, the policy fails.
- The reason why the higher organic composition of this aggregate worsens the crisis is that the extra investments have gone predominantly to the most efficient firms (those with higher organic composition). They, by selling their higher output at the same price as that of the laggards, appropriate value from these latter and eventually push them out of the market thus worsening the crisis.

- (c) In the opposite case, where the organic composition falls as a result of these investments, the ARP rises. But then the Keynesian policy has helped the less efficient capitals, those with lower organic composition and thus lower efficiency, to survive. In this case, this policy *postpones* the slump instead of ending it.

- This shows how unrealistic is the call also by prominent Marxists for a massive wave of state induced capital financed redistribution and/or investments in the present economic predicament as a way out of the crisis.

A further limit of Keynesian policies

- Besides the limits underlined by the Marxist multiplier, state induced redistribution and/or investment policies meet a further obstacle. They are possible when private capital can bear the loss of surplus value (or of reserves). But when capital sinks into crisis, when profitability falls, their financing becomes increasingly problematic. These policies can be applied where they are least needed and cannot be used where they are most needed.

Keynesian monetary policy

- Some Keynesian authors (Krugman) propose to stimulate demand neither through redistribution nor through investments but by increasing the quantity of money. The (Keynesian) assumption is that the ultimate cause of crises is lack of demand. The argument against this view is not so much whether these policies are inflationary (as Austrian economists hold) or not.

- Rather, the objection is that by printing money, one increases the *representation* of (surplus) value rather than (surplus) value itself. The economy cannot restart if the surplus value produced relative to the capital invested is unchanged.
- Moreover, by printing and distributing money, one redistributes purchasing power. But we have seen that neither a pro-labour nor a pro-capital redistribution is the way out of the slump.

- But usually, by ‘printing money’ one understands granting credit. The notion that credit is money is almost universally accepted and yet fundamentally wrong. By creating credit, one does not “create money out of nothing”, an absurd proposition. Out of nothing, one can create nothing. Simply, by creating credit, one creates debt. So the crisis is postponed to the moment of debt repayment.

Capital borrowing

- This is one of the reasons why the state may decide to *borrow* the capital needed for public works rather than expropriating it from capital. But eventually debts must be repaid.
- The Keynesian argument is that debts can be repaid when, due to these policies, the economy restarts and the appropriation of the surplus value needed for debt repayment does not threaten the recovery. But this is wishful thinking.

The solution: capital destruction

- In fact, we have seen that state induced capital financed investments cannot restart the economy. At most, they can postpone the explosion of the crisis.
- Then, if anti-crisis policies are impotent against the slump, the crisis must run its course until it itself creates the condition of its own solution. This is the *destruction of capital*. Only when sufficient (backward) capitals have been destroyed (have gone bankrupt), can the more efficient productive units start producing again on an enlarged scale.

- Thus, if these policies at best postpone the explosion of the crisis, they also postpone the recovery. By postponing the recovery, these policies are an *obstacle to*, rather than being a condition for, *the repayment by the state of its debt*.

- In the present conjuncture, neo-liberal policies, basically wage cuts through budget cuts, are almost universally criticized from a Keynesian perspective, as if these policies would strangle the economy because they depress (labour's) consumption. But the economy grows if consumption rises together with profitability. A greater consumption induced by higher wages would further decrease profitability. Moreover, given the high levels of both state and private debt, wage cuts through budget cuts decrease losses rather than increasing profitability. They can neither increase consumption nor the ARP. Budget cuts are then perceived as the cause of the deepening of the crisis. But austerity is the consequences of falling profitability, an attempt by capital to restore the ARP which however cannot work because it decreases debts instead of increasing the ARP and because it depresses consumption.

- There is no affinity between this conclusion and the Austrian school. The differences are abyssal. Just to mention two out of the many: for the Austrian school the economy, if not tampered with, tends towards equilibrium (rather than towards crises, as in Marx) and government intervention is the cause of crises (rather than being one of the many countertendencies, as in Marx).

- The thesis that state induced redistribution and investment policies, possibly through state borrowing, could start a sustained recovery, provided the scale is sufficiently large, is not only theoretically invalid (see above) but also empirically unsubstantiated. The example usually mentioned is the long period of prosperity that followed WWII, the so-called Golden Age of capitalism. Supposedly, government borrowing made it possible for the US state to finance Keynesian policies and thus to start the long period of prosperity.

Lessons for labour

- In reality, the US gross federal debt as a percentage of GDP *decreased* constantly during the Golden Age, from 121.7% in 1946 to 37.6% in 1970. In reality, the long spell of prosperity was due to reconversion, i.e. to the reconstitution of civilian capital, and to the liberation of pent up purchasing power after the war.

- The above should not be construed as if labour should be indifferent to state induced, capital financed redistribution and/or investment policies. On the contrary, labour should strongly struggle for such policies. But this struggle should be carried out not from a Keynesian perspective but from the proper, Marxist, perspective.

The real meaning of Keynesian policies

- The Keynesian approach considers Keynesian policies as a struggle to improve both labour's conditions and to counter or exit the slump.
- The Marxist perspective stresses that state induced, capital financed distribution and investment policies should not be called Keynesian because of the ideological content of the word. It stresses that these policies may improve labour's lot but are impotent against the crisis. They can at most postpone it.

- But equally important, the Marxist perspective stresses the *political potential* of these policies if, through the struggle of labour for better living and working conditions, the consciousness arises and grows
- (1) that each time these policies are paid by capital, capital is weakened both economically and politically, and
- (2) that labour should profit from this weakness to weaken the yoke of capital.

- From the Marxist perspective, the struggle for the improvement of labour's lot and the sedimentation and accumulation of labour's antagonistic consciousness and power through this struggle should be two sides of the same coin.
- This is their real importance. They cannot end the slump but they can surely improve labour's conditions and foster the end of capitalism.

- Thank you for your attention.