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Suggestions for curing the ills of our  
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## 15. Conclusion

Look around yourselves and you will see evidence that Henry George was correct. All of you could have probably found easier ways to achieve profit and or power; comfort and or repose, than the life tracks you have chosen. I'll guess that a main factor in your choices has been a reaction to the need for justice, not merely utility in human relations. We need to spread that worldview and basis for human action, by giving proper respect when we see it in others; in our writings and talks and relations. And always remember that morality and greater fairness in society are ultimately highly utilitarian. People do (and should!) react to being treated honestly. The ramifications for their society means that justice, in particular basing our money systems in fairness, is a highly useful policy. In this process we can give those who presently obstruct human development for private gain, what they've denied to the rest of us, we can give them justice too.

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## Toward a Non-capitalist Market System: Practical Suggestions for Curing the Ills of Our Economic System

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### Abstract

*The paper focuses on the reform of economic institutions –those of the market mechanism and the financial system, in particular. After introducing the analysis with an historical excursus on the development of economic institutions, the intent here is to propose significant modifications of the present market and financial establishments, which despite their radical flavour, will be shown to be, in fact, no less pragmatic than indispensable to cure the economic maladies of our age. Throughout the modern times, all spokesmen of powerful institutions –e.g., churches, governments and economic elites—have always been keen to recognize in principle that these bodies are never perfect, and that societies assuredly need to take a step back, so to speak, ponder things over and eventually improve them. This is exactly what we set out to do in these pages: namely, we wish to lay the foundation for such an analysis of market developments, and thereafter suggest the remedies for making society a workable economic proposition.*

**JEL CODES:** P19, D49, D39, E43, G29, F02

**KEYWORDS:** Capitalist system, Dynamic competition, Income distribution, Interest rate, Financial institutions, International economic order

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## 1. Introduction

This essay analyses a central question of modern society: how does one best use ‘the instrument of the market’—this being a basic mechanism of organizational efficiency in dynamic economies characterized by a high degree of uncertainty—, in such a way as to prevent the market itself from turning everyone and everything into expendable tools, with consequences that are ever more disastrous for equity and for human dignity?

The purpose here is to envisage the possibility and, more importantly, the necessity of economic forms adapted to human society that are *different* from those that have emerged from the spontaneous transformation of the Western world. Persisting in the denial and ignorance that such a possibility of *change* is indeed possible will inevitably lead to the (often fanatical) conviction that the capitalistic market, with all its degenerations and inefficiencies, is the unavoidable, even if bitter, outcome of institutional evolution—a necessary, teleological fruit of human exertion: ‘the end of history’.

To analyse this topic with the depth and the breath it deserves, we will first sketch a brief account of those institutions and forms of civilisation that in the course of history have promoted the rise and spread of the market, eventually making it into an organizational necessity of modern economies. This account will be concluded by a summary of the pros and cons of the capitalistic market. The subsequent step concentrates on the notion of *competition*, and in particular on the role of the *entrepreneur* and the significance of the rate of profit as a gauge of accountability. This is essential in order to highlight the powers of resilience of the market, and to show its flexibility as an organizational tool with regard to various kinds of ideological options: for instance we will contemplate how it may be extended to either private or public systems of ownership. In section 4 we discuss

how the market may be turned into a mere mechanism for the imputation of costs and efficiency, and this discussion is at the heart of the following proposal for a non-capitalistic market and the merits of its social openness. This argument will then lead directly to the treatment of a defining, and fundamental component of the system, upon which all reformist propositions impinge by necessity: the nature and management of the interest rate and the attending financial system. These are two dominating and interconnected aspects of traditional economic systems that increasingly thwart entrepreneurship and stifle production since they are predicated on a high concentration of economic power in the hands of a social class *de facto* devoted to speculation rather than production. We offer a solution to this problem, and conclude the article with a few considerations on the international order.

The goal here is to devise a coherent reformist agenda articulated in several key points pertaining to the vital nodes of the economic system<sup>1</sup>. This is just a beginning, a first attempt: naturally, given the complexities of the issue, the remedies recommended are by no means exhaustive, but merely indicative of the broad path all humanist forces should undertake together in days to come.

## 2. An Historical Sketch of the Market

In this section, which is devoted to ages in which the market was hardly the protagonist, we will identify the structural obstacles that impeded the development of market relations and the contingencies that eventually allowed those relations, in some instances, to rise gradually and spread all around. We then consider the

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<sup>1</sup> The development on the method of social science exposed in Fusari (2004) may allow a better understanding of this essay.

strong interaction between the growing influence of the market and the rapid pace of social transformation, which has brought the market to become the essential mechanism for efficiency, growth and development.

In ancient times markets were absent or marginal because they were not necessary to the organizational efficiency of social systems; rather, as we shall see, the market obstructed efficiency. The major role played in some ancient societies by individual initiative, critical spirit and the propensity to adventure was much more a stimulus to creativity, scientific research and geographic discovery than it was to the market economy. The economy did not hold a central position<sup>2</sup> and did not attract the interest of students and practical men. Of course, the great empires of the ancient world devoted considerable resources to hydraulic, monumental and military works. However, these were centrally administered, authoritarian societies that suffocated individual initiative, and in particular mercantile activities. Which does not mean that they could not achieve wealth, power and social sophistication: in fact, a stationary-repetitive economy may be efficiently managed by centralized processes and bureaucracy. Indeed, the most advanced societies of the ancient quasi-stationary world were bureaucratic, autocratic and centralized empires, whose neatly ramified branches often afforded complete and efficient control over extensive regions, avoiding thereby the dissolution and fragmentation.

The crises of the two main commercial empires of the ancient world, Carthage and Athens, are good instances

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<sup>2</sup> In the few ancient societies based on the activities of traders, like the Phoenicians and a few other *poleis* situated on caravan routes or along the shore, trading did not engender a cumulative development. Such a failure condemned them to extinction or subordination.

of such a tendency. Those empires were defeated by less rich but more highly structured rival powers. The organizational inconsistencies of the two empires, the avariciousness of their ruling classes, and the resentment of their confederates and subjects, all represented heavy functional handicaps in the static outlook of both systems. But the best illustration of the market's unsuitability to quasi-stationary societies is provided by the experience of the Roman Empire from Augustus to the Antonines. That empire was governed by highly advanced institutions, suitable to the modern world and unique in ancient times. An active and efficient body of public servants authoritatively administered justice, public order and taxation; the remaining public functions were assigned to the municipal self-government of the *decurions*;<sup>3</sup> individual initiative was well represented and taxation low. But the major pride of the empire, the great Greco-Roman civilization with its central idea of circular time, and the marginal role of the economy, the running of which depended on the polarisation aristocracy-slavery, hindered cumulative development and the role of the market.<sup>4</sup> The persistence of stationarity, hence stagnation, transformed the promising decentralized public administration of the empire into a factor of dissolution.

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<sup>3</sup> These were the members of the councils of the urban communities, who were vested with deliberative power and competence on local finance, building, public works, and public utilities.

<sup>4</sup> The enormous economic power of the Roman aristocracy grew over time as a partial compensation for the political influence subtracted to Senatorial class by the emperors and their civil servants. But aristocratic culture disregarded economic productivity and influenced the culture of the merchant class, and slavery made possible the sustainability of such culture. On the other hand, the Christian-Judaic notion of linear time was obscured by the dominating civilization.

So the great crisis of the third century A. C. and an extremely painful process of trial and error drove the Roman Empire toward the bureaucratically centralized, hierarchical society of Diocletian and Constantine the Great. In that society, as in the other great empires, the market was clearly marginalized.

The collapse of the Western Empire –which, unlike the Eastern provinces, was socially and economically dominated by large estate slavery tenancy and a large state subsidized urban populace— resulted in a severe retrogression in the general conditions of development. In this new stage of arrested growth, the body social reverted to a primitive structure governed by familial links: the quasi-familial relations of loyalty on the part of the populace to the descendants of the great Senatorial landowning class, or to Germanic military chiefs, assumed a basic role. No proper State power came into being. The sovereigns of the barbaric states were for the most do-nothing kings, controlled by a military aristocracy. Nor was there any centralized or autocratic empire in fragmented post-imperial Europe. Charlemagne's empire was a kind of "shooting star". After his death, social organization took to the feudal model: a world governed by strong and arrogant individuals, plunderers more than administrators; as Anna Comnena noticed during the transit through the Byzantine Empire of Crusaders' expeditions: these were fighters for the faith, but also for spoils and fortune, "extremely greedy for any kind of gain."<sup>5</sup>

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<sup>5</sup> See A. Comnena, *L'Allessiade* (Stamperia Andrea Molina, Milano 1849). Cupidity was very widespread, even among true believers. The crusaders of Peter the Hermit devastated the Balkans to a surprising degree, pillaging and slaughtering. They greedily ventured into Anatolia, too impatient to wait for support, and were promptly exterminated.

In such turmoil, what became of the market? The Western European world dominated by avidity and the spirit of independence, and well disposed to adventure, favoured a luxuriant efflorescence of mercantile activities. The maritime towns were clever at making huge profits from the Near-eastern conquests and the growing hunger for exotic goods. The medieval Communes that followed, carefully created laws, and institutions suited to trade, and were resolved to defend and extend their independence by fraud, talent and the sword. The economy began to take on a central role; it now wielded progressively political power and came to finance troops and mastermind conquests. Innovations became more frequent, and while they might have appeared at first to be of little importance, they contributed greatly to productive efficiency. Ancient Chinese inventions were adopted; others were rediscovered in the Arab world, which had been driven into decline by Islamic theocracy, despotism and the vice and decadence, as deplored by Ibn Khaldun.<sup>6</sup> The figure of the so-called merchant adventurer arose and the drive for discoveries and profit opportunities intensified.

This triumph of individualism and activism contaminated the intellectual milieu of Europe. Philosophy and scientific investigation flourished. The religious world, cultivated in the monasteries, which held a monopoly of knowledge, now began to court heterodoxy. The spread of heretical groups and then the explosion of the Protestant Reformation made theocracy

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<sup>6</sup> See Ibn Khaldun (1958). He was a great Arab historian and traveller across *dar al Islam* that lived in the fourteenth century. He wrote an important and voluminous history of Arabs, Persians and Berbers, in which he fashioned a peculiar theory of historical processes. Through his creative analysis he identified the cause of the decadence of Arab world in the excesses of absolute power, injustice, unproductive expenditure, nepotism and corruption.

impossible. The idea of linear time, which infused the perception of “becoming” and the sense of expectation, once it became wedded to a pluralistic, decentralized social structure permeated by the individual search for material wealth, ended up fertilizing the soil of commercial spirit and economic activity. A world open to creativity and change wedges its way into history.

Nevertheless, until the sixteenth century, there was no such thing as the self-sustained growth of the economy. Despite the progressive build-up of this pre-modern “dress rehearsal” for capitalism, Western Europe was still less developed than China, though it had a key advantage: entrepreneurship. In fact, the great geographical discoveries of Ming admiral Zheng-Ha in the early fifteenth century had no effect on the centralized Celestial Empire, hostile as it was to businessmen and inclined to isolate itself from the outside world. By contrast, the European Age of Discovery was an epochal turning point, driven mainly by the impetus of merchants and adventurers. The growing dimension of the market began strongly to stimulate labour division and hence labour productivity.

Still, the immense flows of resources that accompanied those events and the appearance of manufactures could not by themselves have averted European society’s relapse into quasi-stationary motion (even if at a higher level of development), or even disintegration and the extinction of creativity, as in ancient Greece. This danger was averted thanks to the immense contribution of science. Henceforth, economic competition would be based even more strongly on innovation—Schumpeter’s “creative destruction.” The era of industrial society began and capitalism was fully established, at last.

*The rise of a dynamic social system made the market a crucial organizational necessity.* In fact, it is impossible for bureaucracy to govern a dynamic

economy, which by definition is characterized by great uncertainty, and which needs a steady supply of creativity and innovation. Bureaucratic organization inevitably leads to the stationary state. Entrepreneurship, creativity and innovation need the market, which is the sole mechanism that can coordinate a large quantity of disconnected initiatives and conflicting decisions in a radical state of uncertainty, and eventually assure their overall consistency while providing adequate incentives for all activities.

The central role of the economy and the need for the market—both of which imply the ontological imperatives of individual action, creativity and inquiry—allowed the progressive destruction of the centralized, authoritarian societies that had submerged the world until modern times. The extremely peculiar causes of this turning point are well exemplified by the case of Japan: a society that, despite many affinities with European feudalism and decentralization, was unable to free itself from stationary motion but relapsed into a centralized Shogun feudalism that lasted until the Meiji revolution of the nineteenth century. This result, starkly different from that of Western Europe, can only be attributed, primarily, to the lack of the capitalistic market.

### 3. The Capitalist Market

This section focuses on the capitalistic nature of the evolutionary process previously discussed. In particular, it underlines the initial propulsive strength of the capitalistic market and proceeds to single out its growing limitations, which appear to form an explosive blend of contradiction, discontent and inefficiency in the present age.

In the eighteenth century, Mandeville emphasized the role of selfishness and corruption in driving society to

prosperity and dynamism.<sup>7</sup> Soon after, Adam Smith's economics celebrated the "invisible hand," a metaphor for the combination of the market with individual interest. Both were right as commentators of their own era. In fact, the robberies and lack of all ethical constraint on the part of merchants and entrepreneurs were crucial to primitive accumulation; they were the prerequisite for the advent of industrial society. Well-governed social orders, like the great empires or Tokugawa centralized feudalism, were unable to promote endogenous growth, which was stimulated above all by the lubricating role of the market and self-interest. However, Mandeville and Smith went too far in asserting that these phenomena represented *natural laws*.

Secularisation proceeded, promoting the theory of separation of economics and politics from ethics, and thus silenced the grumbling of the moralists. Such separation represented an evident scientific error. As a matter of fact, social sub-systems always interact: they cannot be separated. But the scientific mistake operated very well in practice: it eliminated the submission to some ethical rules that contradicted various organizational and functional necessities of the new, modern world. Besides, it stimulated the alluring powers of material incentives and the role of the market. This drift accelerated the completion of the great march towards the *open society*, which gradually smashed the closed and authoritarian civilizations that were still left standing.

The accumulation of financial capital represents a central aspect of dynamic economies: an acute hunger for capital has accompanied the evolution of capitalism

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<sup>7</sup>He was persuaded that «personal vices may be made useful, by a clever government, to the worldly happiness and the greatness of the whole» See B. Mandeville, *The Fable of the Bees* (Laterza, Bari, 2000, page 5.)

from its first steps. In Medieval time, international traders from Italy invented a peculiar institution called *collegantia* to collect the commercial capitals they necessitated. Loan at interest and discounting (of commercial bills) was diffused in Medieval fairs. Banking system came to know a rapid diffusion. Amsterdam, and later London, became the heart of a powerful world capital market. The domination of finance capital had just started. The management of interest rates became the crucial mechanism of the monetary system, and speculative activities gradually ousted production from center stage.

The moral impudence of market relations and standard financial maneuvers soon began to engender disgust and moral disapproval, which were strengthened by intensifying exploitation. This development gave birth, in the realm of social thought, to a great error, well expressed by Polanyi: namely the idea that the market is just one of various organizational possibilities and that it can therefore be discarded in favour of a different one, say, a "redistributive" (Socialist) system. Such a conception found expression in a variety of utopian designs, which were for the most part fuelled by indignation over the infamies of the market and its agents, and which all called for the abolition of the latter. The aims of anti-market utopia, however, never seemed to go beyond the notion of the stationary state and the closed society, which ultimately signify regression to retarded stages of development. This was shown clearly by the most distressing of such utopias, Communism, which aimed to eliminate the market but never escaped its influence, from the early period of the NEP under Lenin's tyranny up to the recent collapse of all the Socialist systems. The methodological equivocations afflicting social theory obscured the fact that the market, entrepreneurship and individual initiative are simply

organizational necessities in modern dynamic economies and the open society.

The only critique of the market based on scientific foundations appears to be the analysis on “market failure,” according to which, the market is in some instances found incapable to act efficiently, in particular with reference to public goods, and when market demand for goods is insufficient to absorb production. As a routine, governments –colluded with business—have encouraged a large expansion of public expenditure to remedy the deficiency of demand, and therefore allow the market to ‘digest’ less troublingly. Yet this routine was gravely flawed from the outset: it disregarded the efficiency of the public sector and of the public administration. This oversight stimulated the birth of an alternative approach that emphasized “government failure,” which, coupled with the fall of “real Socialism” in the East, greatly strengthened the market fundamentalists, and thus boosted the advent of the so-called *new economics*: a gospel preaching absolute free trade and a blind faith in the free market.

Meanwhile, rapid development of communications has allowed market relations to envelop the entire planet with thousands of tentacles, transforming the open society into a *global society*. Thus the free market has become the owner of the world, with the devastating presence of the four modern Horsemen of the Apocalypse: distributive iniquity, growing international disequilibria, social disintegration, and mass unemployment. These phenomena are most acute in the underdeveloped countries, but they do not spare even the heartland of the free market. In the United States, following the trend in the concentration of wealth, the difference between the highest and lowest personal income groups has almost trebled in the last forty years. The earnings of a CEO are almost a thousand times those of a simple workman, while public opinion is

increasingly concerned over the unspeakable abuses of corporate power. The transition in the former Socialist countries has almost always taken the worst of the market economy: privatisation has usually produced massive frauds and corruption.

Everywhere around the world one may see the astounding facility with which the free market makes instruments of everyone and everything. The necessity of the market favours the diffusion of so-called capitalistic ‘ethics’ and ‘civilization’, even if they are not strictly necessary to market institutions. So, an insidious kind of colonization is at work, which people accustomed to different cultural values have come to hate with a passion. As mentioned before, not even the Western world can blindly trust the sorceries of the free market.

A highly dynamic society is obliged to cultivate a diffuse solidarity and a deep sense of cooperation to defend individuals from uncertainty, precariousness, loneliness and frustrations, which rapid social change is wont to inflict on man. Here, contrary to appearance, we have a basic inconsistency of the present historical era with the idea of a spontaneous social order. Today, moreover, the virtues of public expenditure in recreating the structural consistency between production and socialization have disappeared, having the public deficit become a constraint instead of a stimulus to production. As we shall see later, such consistency now requires to make the market a mere mechanism of imputation of costs and efficiency. This is an important new *organizational necessity* of modern social systems. The race for earnings may itself foster the worst misdeeds and has, from a moral standpoint, incredibly destructive power. We have seen that the ability on the part of market relations to furnish incentives, during the march towards the open, global society, was intensified when it came to be combined with non-ethical behaviour. Today it is ever- more indispensable to link market relations to



higher level of ethics. The global dynamic impulse of the separation of ethics from politics and economics in social thought and action is beginning to turn into an obstacle to the growth and development of human societies.

The high level now attained by the general conditions of development and the growing social maturity of the masses make the persistent phenomenon of “power as domination” ever more indigestible, a factor of growing contradiction. The transition to “power as responsibility” is urgent in both politics and economics. One of the great merits of the market is its capacity for automatic, objective and inflexible attribution of accountability for the results of daily economic activity and decisions. But it is necessary to flank this responsibility with an equally objective and inescapable responsibility to the laws governing market relations, so as to avoid, for instance, bribery and corruption, which also undercut economic efficiency. The crucial imperative today is, again, to disengage the market from its inclination and ability to turn all of us and the world at large into its tools.

Let us provide a set of solutions to this problem.

#### **4. Entrepreneurial Role and Profit Rate. The Public and Private Spheres Within the Working of the Market**

In this section we will identify some precise organizational requisites for the establishment of a wholesome entrepreneurial economy. Such a careful definition will enable us to combine our revisited model with diverse ideological options.

We have just seen that modern economies cannot do without entrepreneurship and market relations; and that the market’s automatic, objective attribution of the entrepreneurial responsibility for action and decision is a precious device. Both in private and public companies (operating for the market), the only reliable indicator of

success and hence of responsibility is the profit rate.<sup>8</sup> All other significant indices refer only to particular aspects of entrepreneurial action; they are partial and may accordingly become misleading.

Various economic theories maintain that the entrepreneur is interested in total profit, not in the profit rate. But total profit is not a ratio of return; therefore, it does not represent an indicator of entrepreneurial success. The search for total profit demands that investments be ranked on the basis of their earning rate, if the global activity of the firm is constrained (as it always is) by the availability of some factor of production.<sup>9</sup> But the profit rate is a good indicator of success only if it is obtained in a competitive market, not through monopoly, for competitive markets force the entrepreneur to engage in a ceaseless struggle for profit, and thus bind him to his function and his responsibilities.

To avoid misunderstandings on this crucial matter, an important specification on the notion of competition is required. The competition based on the entrepreneur’s search for profit is the one considered here. It may also be intended as a combination of Kirzner’s “market process” and Schumpeter’s “creative destruction.”<sup>10</sup> This notion of competition seems to be the only appropriate one in a discursive analysis of modern dynamic economies characterized by innovation and uncertainty. But a complication arises: successful innovation causes temporary monopoly. The complication is only apparent, however: in fact, an innovator’s monopoly does not

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<sup>8</sup> The well-known Lange and Lerner’s rules, that should drive the entrepreneurial behaviour in market socialism, make sense only in a static economy, that is excluding innovation and uncertainty. Therefore, they cannot be referred to reality.

<sup>9</sup>This clearly appears from the formulation of a problem of optimisation under the constraint of the available entrepreneurial skills (or some other scarce factor).

<sup>10</sup> See I. M. Kirzner (1973) and J. A. Schumpeter (1954).

cause restrictions to competition, rather it is the engine of dynamic competition. Therefore, anti-monopolistic vigilance must not target this kind of monopoly, which will vanish as soon as the incumbent innovation will be undermined by a superior one –and that is, as soon as the benefits for the community deriving from the original innovation cease. In short, an innovator's profits express the success achieved in the performance of entrepreneurial function, not a privilege.<sup>11</sup>

Under this set-up it will be important to prevent that entrepreneurs falsify the accounts with a view to showing larger than actual profits, and so deceive bankers and other financiers. In public firms, such falsifications may also be triggered by the aim of avoiding blame. The greatest watchfulness is therefore required.<sup>12</sup> Some standard corporate accounting

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<sup>11</sup> In Neoclassical economics, price competition results in allocative efficiency. However, this is a result of comparative statics as opposed to a dynamic process. This is like taking a series of pictures--the economy that results is stationary: it does not move--the process by which we go from one point to another is an illusion, just as a motion picture provides the illusion of movement. However, since the movement from one point to another is not considered, the efficiency that results is one that is based only in the moment and is, thus, a stationary efficiency. The notion of competition relevant in this context does not imply such stationary efficiency. Indeed, neoclassical competition is almost senseless; a stationary economy does not need the market.

<sup>12</sup>In workers self-managed firms the falsifications are stimulated by the interest of workers to increase their earnings. A way of exaggerating profits may consist in the underestimation of capital depreciation and, on the part of banks, in the concealment of the losses due to the insolvency of the financed concerns. But these manipulations (directed to hide losses) will depress profit rates of the successive years, since they will cause a fictitious growth of capital, and will thus force the firms performing those tricks to feed a growing fraud

procedures have been devised at the EU level to facilitate monitoring and gauging corporate profitability. Other controls on corporate results are used for tax purposes. It is important to perfect them. We shall see that the main difficulties in auditing business accounts are due to the confusion and complications of international relations. The situation is aggravated by widespread bad faith. In effect, the alarming frauds reported in the press are possible only because of the "kindness" of the authorities, which turn a blind eye; such complicity must be harshly repressed.

The basic characteristics of the market as set forth here do not, at first glance, imply any theoretical innovation. However, their strict essentiality has substantial analytical value. Our model implies the unrestricted possibility of combining the market mechanism with a large number of different institutional, ideological and relational forms. In particular, our concise analytical foundations allow us to deal with the problem of property free from prejudice, inhibition and mystification, making evident that private ownership may be severely limited by public firms operating in the market without damage to efficiency and with some important advantages for social justice and the control of the overall rate of accumulation, and thus of aggregate demand. For in this kind of firm, profit serves only as the indicator of entrepreneurial success, which should determine whether the managers are kept on or discharged, and not as the vehicle for personal enrichment or unconstrained speculation.

As is well known, private property is one of the institutions that have vaunted, in the course of recent centuries, the greatest merits and demerits. It has been at one and the same time a great source of freedom and

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over time, which would become increasingly more difficult to conceal.

of oppression. It has been the main barrier against the stifling domination of public institutions, it has stimulated pluralism, it has been an important source of individual incentive, and it has constituted an important defensive shield of personal independence. At the same time, it has greatly stimulated and inculcated greed and it has been a formidable means for the exploitation of man by man, and for countless other abominations. Moreover, it has fostered an enormous concentration of power. How are we to separate virtues from drawbacks, to preserve the former and eliminate the latter?

This problem largely coincides with the question of delimiting the appropriate sphere for private property, while guaranteeing freedom and justice for all citizens.

We can set out a general principle: *private property should be preserved in so far as it promotes productive efficiency, the satisfaction of citizens and the full appreciation of their qualities and aspirations, without implying the creation of dominant positions.* Both durable and non-durable consumption should be included in the sphere of private property, in particular homes, gardens and intensively cultivated plots of land. Moreover, small farms, craft and commercial enterprises, whose success is difficult to monitor and hence to control, should be privately run. For efficient performance, these firms need the dedication that comes from private ownership and private appropriation of profits. And as these firms are small, they do not imply dominant positions.

In this economic system, everyone can consume what he wishes, as the search for profit will push firms, driven by prices, to satisfy consumers' preferences. Here the question of new goods and the manipulation of demand through advertisement arises. The introduction of new goods and services is of critical importance for consumers since it broadens their range of choice. Furthermore, in the absence of new products, consumption would be saturated and the economy

would stagnate. The entrepreneur produces new goods if he thinks they will be bought. But new goods require advertisement to inform people of their existence. What must be condemned is false, misleading advertisement, not informative publicity. It is undeniable that the purpose of publicity is always to influence consumers. But the purpose of any message whatever is always to influence the listener. The only guarantee against the risk that such influence may create a dominant position, which jeopardizes freedom, is pluralism.

### **5. The Cycle of Production and Distribution within the Market Operating as a Pure Mechanism of Imputation of Costs and Efficiency**

We are about to broach the core of our reformist proposal. Its goal is to delineate the widest possible bounds of social equality, in ways that are consistent with freedom, efficiency and development: in other words, we are seeking to find the preconditions guaranteeing the highest degree of social equality that modern society may achieve.<sup>13</sup> The pursuit of these aims requires the transformation of the market into a pure mechanism of imputation of costs and efficiency. Such a transformation needs the establishment of a special fund; therefore some preliminary considerations are necessary to clarify the nature of this fund.

The rapport of economics and social science vis-à-vis the market is twofold: on the one hand, the market has been considered as a potent vector of immorality, instability and social precariousness, and because of

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<sup>13</sup> The treatment of this topic bears some resemblance to J. Rawls' investigation (see J. Rawls 1971); but our analysis is more specific and operative than that of this author, it being specifically concentrated on the concrete management of market relationships.

this, many have called for its wholesale abolition; on the other, the market has been understood as an institution indispensable to the efficiency of production, which, at most, is allegedly thought of requiring but the complement of social welfare to run perfectly. We saw that the first course of action is completely senseless in modern dynamic societies, while the second perspective appears nowadays utterly insufficient.<sup>14</sup>

We wish to offer a different model, which operates a profound transformation of the market mechanism, and which is predicated, among other things, on the creation of a special fund. This fund of community wealth should enable the system to conjugate the achievement of the highest possible productive efficiency with freedom in the distribution of income. More precisely, it will be proved that this fund is crucial to the pursuit of four main aims: business efficiency, distributive justice, full employment, and individual autonomy. As far as we can tell, there is no example of such a fund in the present and past ages. Let see how our suggested model functions by starting with production.

In this model, the firm buys the goods, factors of production and services required by its productive decisions on the market, at market price, just as it does today. But it does not pay wages; instead it pays the price of labour as computed by work offices on the basis of the demand and supply of the various types of

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<sup>14</sup> The debate on market Socialism in the years between the two world wars, was hinged on the hypothesis of a stationary economy, which does not need entrepreneurship, and thus made room for the formulation both of a centralized model of the economy, as that elaborated by E. Barone in the essay on "The Minister of Production in the Collectivist State," as well as of that of a decentralized model of market socialism, with the manager's decision-making simply dictated by Lange, Lerner and Taylor's rule. (See A. P. Lerner 1938, O. Lange and F. M. Taylor 1938).

labour<sup>15</sup> into what we may call a "fund of community wealth." However, the firm may pay incentives to its workers and also overtime, if it deems it advantageous.

Moreover, companies will pay into the fund a penalty for any damages to the environment; conversely, they should receive contributions for any social benefits deriving from their action. Firms are also taxed. Finally, they may have to pay into the fund a surplus over regular labour cost to assist the transfer of workers from the district of origin. The purpose of this is to stimulate capital to flow toward labour, so as to minimize the effects of uprooting, congestion and urbanization generated by migration.

At the end of the production phase, the firm will sell output at market prices. With the proceeds, it will cover constant and variables costs, including capital depreciation and costs on borrowing, as well as taxation. The difference between revenue and costs, divided by capital employed, yields the profit rate.

In addition to incentives and overtime paid directly by the firm, workers are entitled to a portion of the fund of community wealth. The determination of this portion and its distribution among social groups will follow criteria defined outside the firms, in the political sphere and through negotiations among social groups and their representatives. The share of each occupational group in income distribution may also depend, in part, on supply and demand for each kind of labour specialization; that is, each group's share may be augmented or decreased, depending on whether demand for that type of labour is greater or less than

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<sup>15</sup> As is well known, demand and supply give, by themselves, relative prices. So, to obtain the prices of nominal labour it is necessary to refer to some labour price expressed in money units or, taking variations, refer to initial prices expressed in money units.

supply. In this way, the balance between labour demand and supply will be fostered by variations of supply, not only by the reaction of demand to changes in the price of labour. Each worker will be entitled to receive, from the fund of community wealth, a compensation proportional to his working time (but not overtime work, which as noted is paid by the firm) multiplied by the hourly compensation for his skill. To reduce transactions, firms themselves may pay this compensation, deducting it from their payments to the fund of community wealth.

At the end of each year, along with the share of output to distribute to labour in the next year, the average gain in labour productivity will be calculated and the share of that increase to be allocated to labour income and the share allocated to a reduction in working time, will be set. This allocation converts technological progress into higher labour income and free time, not unemployment.

People look for jobs by direct contact with firms and following the suggestions of labour exchanges, which have the knowledge of the demand and supply conditions for various skills (because they monitor demand and supply in order to set the price of each skill that firms have to pay into the fund of community wealth). Everyone chooses the job he finds more gratifying (by the type of activity, responsibility, distance from home etc.) and, if he is satisfied, he will keep his job; otherwise he will continue to search for more satisfactory employment. In case of collective dismissals, due for instance to a firm's closing or downsizing, the dismissed labourers will receive benefits for the time needed to find another job.

We can see that this model does not consider labour as a commodity that wage earners sell to the firm but as a service to productive system that entitles the worker to share in income generated. To prevent people from choosing not to work, in fact, the principle must be that

except for those unable to work, the condition for a person to share in the community's income is that he be employed.

In this organization of production, large-scale long-term unemployment is prevented by the perfect flexibility of the price of labour with respect to demand and supply for various skills. As the price paid by firms for the use of labour skills is determined by the labour exchange on the basis of supply and demand, a labour glut would drive down its price and cost, and thus stimulates firms (in the search for profit) to employ more labour and adopt capital-saving technology. The opposite happens if labour is scarce. This should push labour demand and supply toward equilibrium<sup>16</sup>. The tendency is strengthened if the education system produces versatile workers, enabling people to find various kinds of gratifying jobs. But to move the economy toward full employment it is also necessary to pay attention (to this we will return in the next section) to guaranteeing the equilibrium between aggregate demand and supply. This need is particularly strong in modern dynamic societies, with their continuous local and global changes and adjustments. Even more, one must consider that knowledge and its evolution come largely from experience;<sup>17</sup> so that people excluded from the productive process are also excluded from important channels of knowledge and will be increasingly unable to avoid marginalization and alienation.

<sup>16</sup> Sraffa's demonstration of the re-switch of techniques is not relevant in this context, it only shows the erroneousness of the notion of average period of production and of the explanation of the interest rate on the basis of capital productivity; moreover, it makes the hypothesis that wage rate is exogenous, that disregards the relation between wage rate and the supply and demand of labour.

<sup>17</sup> M. Polanyi's pioneering insistence on *tacit knowledge* has provided a deep and extensive illustration of this aspect.

It may be useful, at this point, for a better comprehension of the proposed revision of market dynamics, to work out a more extensive critique of some important aspects of the existing economic systems and ideologies, in the light of this very model.

If, as in the capitalist order, the distribution of income between labour and capital is the result of the clash between wage earners and firms, unemployment cannot be eradicated. For employers, to counter unions and working people's demands, do, in fact, use the infallible weapon of unemployment. If profits are low or firms incur losses, dismissals rise to crush labour's pretensions. And in dynamic economies, firms may also try, with the help of technical progress, to save on labour where it causes rigidities. It is senseless to found protection of labour on laws, norms and rules that oppose the mobility of labour: indeed, such legislation is one of the key impediments to the increase in employment.

It seems clear that the establishment of a fully flexible labour market, which is indispensable in modern dynamic economy, *requires the abolition of wages set at the company and collective bargaining level*. This is all the more urgent in that ordinary collective bargaining does cause inefficiencies in the use of labour and make unemployment physiological. Uniformity of national wage agreements and some other rigidities swell the underground economy in the areas where labour productivity is too low for the national wage rate. These illegal activities allow a fierce exploitation of workers, who have no protection whatever. And the worst of it is that this underground economy is often the only alternative to unemployment.

Trade unions must seriously consider the severe restraints on their bargaining power. They may win as long as the claims of labour lubricate the entrepreneurial system, as wages, increasing in step with productivity gains, stimulate consumption, hence sales, and

eventually lead to an improvement in the condition of the working in the name of social peace and efficiency. But as soon as profits fall, unions find it impossible to force employers to pay higher wages. In substance, the game of wage bargaining is always dominated by the employers, who are most often propelled by competition, avidity and unscrupulous behaviour. It is surprising that trade unions, whose function is to defend labour, have not understood that the root of exploitation is the institution of wage labour itself. It is a misfortune that the distribution of income is so largely determined by wage earnings.

Conflict between labour and capital over wage rates is the worst possible method of income distribution and works as a powerful obstacle to production. The task of firms is to produce material wealth and create jobs. They should be able to do so without being plagued by the perennial conflict with labour, which may be seen as an inappropriate social conflict since it takes place in the wrong place. Income policies to remedy the conflict demonstrate the failure of the company wage approach. They are a rather tortuous way of establishing some kind of income distribution more rational than that implied by the "labour market". *It is crucial to bring income distribution outside the firm, as far as this is possible. This is indispensable to full employment and company efficiency consistent with social justice and individual autonomy. Trade unions should oversee health and safety at the work place. They should fight for the distribution of the fund of common wealth, but not for the company wage.*

Let me also point out that the idea of the workers' self-management<sup>18</sup> of the firm is mistaken. And the

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<sup>18</sup> Where «workers have control over the production process in the enterprise in which they work, since they have ultimate authority, one-person, one-vote, on the enterprise itself» See

workers' remuneration based on firms' results is a vehicle of inequalities and managerial degeneracies. Firms must be managed by entrepreneurs, and must not be involved in the struggle over income distribution. Entrepreneurs' ability in decision-making and innovating must not be constrained by the decision-power of incompetent persons. The entrepreneur must be responsible in terms of results, i.e. profit rate, not subjected to the command of a non-entrepreneurial body. Besides, the rational organization of the economy requires that firms pay for the resources they utilize, including labour, at prices determined by supply and demand. This is a fundamental rule of efficiency, indispensable both to rational use of the resources available and to defeating unemployment. Income distribution is a totally different matter, one that concerns society as a whole. The usual forms of wage bargaining obstruct efficient utilization of resources and prevent far-seeing policies of distribution of wealth. Such bargaining is the product of spontaneous evolution, a sort of "primitive" organizational form of society. An advanced society should be able to supplant those institutions with better thought-out organizational forms.

Moreover, the strict link between the production and distribution of income -or, more precisely, the fact that the distributive conflict affects business accounts, seriously undermines the firms' investment, as well as economic growth and employment. Aggregate investment must be determined by the community and as part of the process of income distribution. This aspect will be clarified by discussing how firms should be financed.

In conclusion, it should be clear that income distribution concerns the entire society and that even

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D. Schweickart, in *Market Socialism* (1998), edited by B. Ollman, Routledge, New York and London, p. 127.

production is a social entity since it depends on productive forces engendered by society, such as techniques and knowledge. Some ingenious theories of exchange value have long maintained that there is an unbreakable connection between income production and distribution. But no such connection exists, except the part due to incentives and the fact that income distribution influences production through the propensity to consume.

In particular, it is senseless to attribute to exchange value an ethic-ideological content as, for instance, the labour-value theory does. The statement value=labour makes some sense only in a stationary economy. In an economy based on innovation, wealth is, for a large part, a result of creativity, genius, and of the entrepreneurial search and intuition. Price is, therefore, a completely different thing from labour-value, and there is no bridge between the two. Really, exchange value displays only the mere functional price role. Precisely, it acts as an indicator of productive opportunities and relative abundance, and as a means to make homogeneous a multiplicity of commodities physically different from each other; its role is thus to facilitate comparison and exchange among these goods. So the ethic and ideological flavour of the labour-value hypothesis, with its implications on income distribution, expresses not only a limiting but also a senseless formulation of the much wider ethical and ideological problem.

The organization of production, distribution and exchange as discussed here attributes a social content both to income production and to distribution. Moralists and social reformers have always considered the market a gymnasium for corruption and aggressiveness, a place of violent contrasts among men, an open space for selfishness and fraud; in brief, it's been depicted as one of the worst instruments of domination, oppression and exploitation of man by man. But we have seen that the

market can be shorn of these unpleasant attributes and transformed into a mere mechanism for the imputation of costs and the stimulus to efficiency through prices, which serve to signal the availability of each commodity. We have also seen that the market mechanism, aided by competition, and combined with a profit rate as an indicator of success (which, as such, allows accountability) can be a highly effective mechanism for stimulating efficient decision-making and management in the absence of monopolistic privileges and under the clear and inescapable rule of law (designed to prevent bribes and other abuses). *The disconnection of the market mechanism from the struggle for income distribution makes for efficiency, individual initiative and social justice, and may thus be relied upon to turn selfishness into healthy rivalry.*

## 6. Interest Rate, Production Financing and Effective Demand

A reformist agenda aimed at the overhaul (if not the transformation) of the capitalist economy would be clearly incomplete without a critique of the most capitalist trait of all: the rate of interest and the rhythm of financial capital. By clarifying the nature of these instruments' role, we will open to the door to a reform of the process of capital accumulation and of the system of corporate finance.

The rate of interest has been considered, in the course of history, as an unjust appropriation of revenue by capital owners. The dispute on its permissibility reached a paroxysm in the Medieval age—in times marked by the florescence of mercantile activity—and was mainly driven by the conflict that arose between Christian ethics and the business drift. The phenomenon of interest continued to loom largely throughout the turbulent transition that led to the advent of the modern

world: and the tragic irony is that this turbulent episode, from an organizational point of view, turned out to be a gigantic, sad waste of life and time, as shall be seen hereafter.

The suspicion of there being foul play and manipulation behind the eternal vicissitudes of monetary dynamics seems corroborated by the spasmodic variability of the rate of interest in the course of history; rates always appear painfully high within societies chronically afflicted by misery and stagnant production. Homer has dedicated a ponderous study to the history of interest rates.<sup>19</sup> The first development of banking, in Medieval Italy, acted like a brake on the surge of interest rates, which indeed fell in this country to levels between 10 and 20 per cent, while in the British isles and Germany they shot to levels as high as 100 per cent. In the late fourteenth century, Italian interest rates on commercial loans hovered around 8 per cent, with a minimum of 5 per cent, and in the fifteenth century an average of 5 per cent prevailed in Germany. A century later, interest rates between 4 and 12 per cent were frequent in Italy, Antwerp and Lyons. The historian C. Cipolla has documented that the Genoa's financial powerhouse, the Banco of San Giorgio, charged interest and discount rates of 5 per cent in the fifteenth century and little above 1 per cent a century late<sup>20</sup>. The wars of the sixteenth and seventeenth centuries caused a rise of the rates, but the seventeenth witnessed a new fall: in the Netherlands interests reached 4 per cent and, by the end of the century, 3 per cent. The incessant development of the banking system was the main cause of these decreases. With the advent of the financial leadership of England, in the eighteenth century, long term government bond yields declined in that country

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<sup>19</sup> See S. Homer (1996)

<sup>20</sup> See C. M. Cipolla (1980)



towards 3 per cent and the usury laws reduced the maximum rate of interest to 5 per cent. In the nineteenth century, Britain's long-term interest rates stabilized at around 3 per cent, while government bond yields reached 2 per cent by the end of the century. The wars that followed caused the rates to rise again.

This course of business shows an inverse correlation between prosperity and interest rates; contrary to Homer's opinion, it does not give the causal direction of the two phenomena; but the association of these is meaningful. True, low levels of interest stimulate growth, and they often stand thereby as an expression of prosperity. What is more important, however, is that since interest rates decrease with the development of banking, their level and their very existence come indeed to depend on the characteristics of the credit system itself.

It is worthwhile to emphasize that interest basically represents a deduction from profit; and it may partially be discharged at the expense of wages, which is a sure way of exacerbating social conflict. In any case, interest stifles entrepreneurial initiative. Can such an impediment to entrepreneurship be eliminated? Can the ensuing deduction from labour-income be eliminated? Complex issue—marred by a host of misconceptions.

To begin, problematic is the moralists' and the political economists' insistence (from Aquinas to Marx) on denying interest on the basis of the labour theory of value<sup>21</sup>—a theory whose ultimate purpose seemed in fact that of shielding the exaction of interest. As set out earlier, such a theory is senseless. Therefore, the alternative justification for the rate of interest as the just

<sup>21</sup> In the *Tabula Exemplorum*, a manuscript of the thirteenth century, it is written: «All men abstain from working in Sunday days, but usurer ones work incessantly». See J. Le Goff, *La borsa e la vita*, Laterza, Bari 1987, p. 24

fruit (reward) of capital productivity—indispensable to the equilibrium between the supply and demand of capital—could easily gain ground (as in Neoclassical and Austrian theories). But that justification is contradicted by a simple remark: capital productivity needs technical progress,<sup>22</sup> which, for its part, has almost nothing to do with financial capital. Afterwards, the Sraffian discovery of the phenomenon of the 're-switch of techniques' (that is the possibility that a rise in the rate of interest may imply an increase in the intensity of capital, instead of a decrease), undermined the thesis of Böhm-Bawerk's average period of production, finishing off once and for all the fashionable models of capital productivity built upon Robinson Crusoe's utopia.

There exists a reasoning capable of solving the debate on interest and usury at once. We ask: is interest strictly necessary for productive and organizational efficiency? If it is not, the existence (and exaction) of interest is unnecessary, and we may thus safely conclude that interest represents an arbitrary and artificial form of income pocketed by the financial cartel. Is this the case?

Tily has written: 'If there is no necessary limit to the volume of credit/debt that can be created then it is essentially a free good. A rate of interest is a price, and prices are paid for scarce resources.... Interest becomes a social construct, to be manipulated according to the mandate, principles or interests of a country's authorities'.<sup>23</sup>

I argue that we need an argument somewhat more stringent in this regard.

Interest has not much to do with the equilibrium between supply and demand of capital. As a matter of

<sup>22</sup> In the absence of technical progress, the accumulation process would push capital productivity toward zero.

<sup>23</sup> See G. Tily (2004), pp. 8 and 13.

fact, far more than on interest, saving depends on the amount of income gained and therefore on the level of production. And, on the other hand, the entrepreneurs' demand for capital depends on entrepreneurship and the state of business, which is mainly expressed by profit expectations. The argument that the rate of interest is necessary in order to prevent 'over-investment' and the concomitant waste of capital is belied by the fact that such a role is *as a rule fulfilled not by the interest rate but by profit rate*, that is by (1) the entrepreneurial search for profit—i.e., the tendency to extract the highest rate of profit from investment—, and (2) by the gauge of accountability role of the profit rate (as discussed in section 3). All of the foregoing implies that the role of interest is simply to throttle entrepreneurship and to subtract income from distribution. It is, therefore, evident that, in principle, the share of income to be invested may be determined by the community abstracting from interest, and that, being the profit rate sufficient to impose a judicious use of capital, it is perfectly possible and efficient to share financing among the entrepreneurs at zero interest. *In sum, there are no technical impediments to the abolition of interest rate through legal prohibition, i.e. by defining as usurious a positive real interest rate.*

Of course, within of a free international financial market, there would need to be a concerted agreement to abolish interest everywhere across the world. However, zero percent might encourage the tendency to hoard money; but this could be opposed through a low rate of inflation or some sort of Gesellian demurrage scheme on cash money. At any rate, nowadays the tendency to hoard seems to be almost irrelevant, since the variety of modern banking services manages to keep private consumption flowing in a perennial, and tumultuous flow. It is indeed remarkable that on the shoulders of a variable, as unnecessary, if not wholly

pernicious, as the interest rate, has grown an enormous, complicated and rather obscure economic body mainly devoted to speculation and entirely responsible for all the serious shocks and malfunctions of the global network.

There remains, at this point, to try to delineate a blueprint for a financing system of production shorn of the negative and pervasive presence of interest—a blueprint capable, among other things, of clipping the wings of financial capital, stimulating entrepreneurship and contrasting the deficiency of global demand-. A discussion on the procedures to modify the banking system in accordance to what will follow is not relevant in this context, and a detailed analysis of the tricks and abuses of that system may form the theme of another paper. The important point is, at this juncture, to stress that the central function of the banking system, when it comes to fund production, needs to be radically modified. Financial capital was born not to serve production but to enslave it, and exploit the toiling community into the bargain. This distortion needs to be redressed at once. My proposal, born as a reaction against the undue appropriation of wealth perpetrated by the financial oligarchy, is presented here in a fashion as simple and transparent as possible.

Every year the community should define the share of value added to assign to consumption and investment, and to investment in selected strategic sectors. After that, care must be taken to ensure, through stimulus and instructions to the banking system, that these prescriptions are executed, as each investment is at the discretion of the businesses.

The capital required by the firms will come, in the first place, from profits. The uninvested portion of a firm's profits may be set aside for future investment. But the financing of capital must generally exceed the reinvested profits, so as to allow the formation of new firms and the

financing of the firms' investment plans in excess of gross profit. Such extra accumulation may be covered in part by private saving, which should yield a real interest rate of zero percent.<sup>24</sup> But savers should not be allowed to buy shares directly, since the stock exchange is much worse than a gambling house, as we shall shown in the next section. The rest of the funds required to achieve the planned rate of accumulation will be provided by the fund of common wealth, which should channel the residual quota to the banking system, to be distributed among firms.

Each bank's application to the fund for resources should be judged on the basis of the profit rate. In fact, bankers must be obliged to operate as entrepreneurs, and their commercial tenure must depend on business results. The more successful they are, as expressed by the profit rate, the more capital will be granted by the fund of common wealth via their commercial bank. Banks' profits should derive from the prices of the services that they offer to their customers; competition should keep these prices low.

A substantial feature of such a reform would be the creation of a mechanism directed to the achievement, through the firms' investment, of the yearly rate of accumulation projected by the community, so that to avoiding or reducing substantially the possibility of a deficiency of global demand. It would also act as a stimulus to entrepreneurship. A major condition for the effectiveness of the mechanism is that *bankers provide sufficient credit to firms to achieve the community's projected accumulation rate*. Therefore, if the banks'

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<sup>24</sup> A real interest rate of 0 per cent on saving would actually be a bargain for savers. These in the course of time have generally suffered a continuous devaluation of their savings owing to inflation, fraud and robbery, which in turn are mainly caused by speculation on financial markets.

requests for capital do not exhaust the fund set aside for accumulation, the difference should be assigned compulsorily to banks (say in proportion to the amount each has requested), for distribution among investing firms. This implies that, if the propensity to invest is low, banks will be forced to lower the prices for their services so that all the funds allotted to them for investment may be placed with the applicant firms. Vice versa, if the amount of capital provided by the fund of common wealth is lower than the total applications of banks based on the firms' borrowing, the negative difference will be deducted from those requests, in inverse proportion to their profit rates. This guideline of equality between the allocations for saving and investment is of crucial importance for the control of aggregate demand; in particular, it moderates the cyclical effects of entrepreneurial euphoria or pessimism. Moreover, it stimulates entrepreneurship since, when demand for credit is slack, firms may obtain inexpensive loans, as banks are required to loan funds up to the accumulation target. So banks are induced to make golden bridges to entrepreneurship, as it were.

If the propensity to invest is low, the duty to attain the established aggregate rate of accumulation may cause heavy losses to the banking system. But this does not represent a problem for public firms, for which the profit rate is only an indicator of success; in fact, the relative degree of success may also be expressed by the inverse of the rate of loss.

## 7. On the International Economic Order

On the international plane, the absurdities of capitalism – and the urgency of a remedy therefor – appear even more starkly than do as when contemplated from the national angle. In fact, the growing integration of world markets, which has given rise to the global

society, multiplies the distortions, opacity and larceny so characteristic of the “free market”. Speculation shifts enormous masses of capital instantaneously around the world. There isn’t any supranational authority deputed to discipline these activities or prevent the crises provoked by such massive transfers of ‘hot money’. Some codes of conduct have been devised as remedies, but unfortunately speculators are clever in crafting tricks to elude them. Moreover, the evolution of financial instruments and markets systematically makes these guidelines obsolete. In effect, it is most difficult to obtain reliable information and craft control instruments in a sphere dominated by uncertainty and rapid change to an extraordinary degree. As a consequence, the concentration of enormous wealth in private hands enables the holders to carry out gigantic frauds, e.g. the sale or dismemberment of healthy concerns at very low prices through manufactured crises. Public ownership of large companies and the model of accumulation set out above would greatly facilitate the exertion of controls and impede speculation.

It is most desirable to deter or prevent savers from engaging themselves in speculation in a landscape full of snares like the international capital markets. Firms should also be discouraged from dabbling in speculation, which distorts and denatures the imperatives of production and the accountability role of the profit rate.

The vices of the international market are aggravated by the selfish myopia of international economic institutions –those institutionally appointed to aiding countries in economic difficulty, usually the less developed economies. The so-called Washington Consensus hinges on three recommendations: privatisation, austerity and openness to the international market. But it is short-sighted as well as cynical to require that, to get aid, the less developed countries must enact policies to balance the budget, put their

international accounts back in order, open up the international goods and capital market, and proceed to privatise all that is public. Macroeconomic stabilisation centering on monetary and fiscal restrictions, which free-trade and the free capital market make particularly harsh, yields high interest rates and the contraction of demand, both of which throttle entrepreneurship and force large-scale bankruptcy. All this reduces output and employment, and increases the share of the population dependent on welfare. The disaster is completed by usurious interest rates on short-term loans, which must be complemented by reserve funds yielding much lower interest rates. During the 1997 crisis in East Asia, the IMF ratcheted up its rate by 25 points: a real disaster for production. Again, it is disheartening to see how interest, a variable that is technically useless, comes to play such an important and destructive role. Significantly, an economist well versed in the operation of international economic institutions like Stiglitz, has harshly criticized those policies.<sup>25</sup> These avoid the true problem, i.e. rebuilding the economy by stimulating efficiency and a sense of duty predicated on a system of clear responsibilities. The promotion of entrepreneurship, and public entrepreneurship in particular, is ignored, while privatisations are often nothing but the theft of public capital. In the recent past, various underdeveloped countries have tried to stimulate economic growth by promoting state industries through central planning. The failure of those efforts opened the door to privatisation. Many State industries in Russia ended up in private hand almost for nothing, even when they could have operated efficiently as public firms, had they been subjected to the accountability of the profit rate and the associated restructuring process.

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<sup>25</sup> See J. E. Stiglitz (2002).

The policies enforced by the international institutions have had disastrous effects in the underdeveloped countries, where an entrepreneurial spirit is generally lacking and the ruling class is much more prone to dissipation, robbery and oppression than to production and innovation. With their systems of patronage and clientele they have perpetuated a corrupt power structure and condemned their masses to hunger.

Production should not be stifled by the class conflict over distribution. It should not be disturbed by the bitterness, the agitation and the despair of underdeveloped countries, or be troubled by unrestrained speculation, mainly to the detriment of working people. International institutions should not offer aid to keep big speculators from going bankrupt. Instead, they should ask, as a condition for aid: systems of accountability based on well-defined criteria of success and, in synthesis, the creation of an efficient, transparent system of economic power capable of production and administration, in lieu of governments dominated by adventurers, arrogant dictatorships, or confusing systems of law that only encourage abuse.

## **8. Conclusion**

One of the chief economic problems of the West has been its increasing reliance on a strange sense of sublimated superiority, which it has erroneously imputed to the most proximate origin of its wealth: the capitalist market. The inference is mistaken in that the source of this wealth, whatever the merits and demerits of its nature and uses, lies in human ingenuity rather than in the capitalist machine, whose essentially constrictive and feudal countenance has come, fraudulently, to represent western economy as a whole. But capitalism is not western inventiveness as a whole; it is but a proprietary scheme that has usurped all the fruits of

western creation. And this tragic *qui pro quo*, has led the West to clash violently with the rest of the world. In truth, the capitalist system is the source of so many disadvantages to the westerners themselves: namely, social injustice, poisoned labour relations and the threat to human dignity, social and geographical disequilibria, the wideness of fluctuations, the sorceries and distortions promoted by the hegemony of finance capital, and finally the smothering of entrepreneurship, freedom and growth.

The present essay has attempted to show a possible way to remedy these ills, in particular the pervasive and distorting influence of the current market and financial systems. Our aim was to devise a model that couples efficiency with social justice, structural consistency with innovation; a system able to eliminate speculation and unnecessary (if not senseless) strife, while preserving the conflicts implicit in the very functioning of a dynamic society, such as the battle between innovators and conservatives. And we have shown that a proper functioning of the market is not inconsistent with man's noble propensities, and that it may very well reduce fraud and greed.

The necessary set of conditions to achieve this goal consists of: 1) the reduction of the market to a mere mechanism for imputation of costs and of efficiency, 2) an expansion of the sphere in which public firms are allowed to operate within the market, 3) and a drastic reform of the banking system. More in particular, we have dwelled on: the essential role of the profit rate as an instrument of accountability for all concerns (public and private); the means of re-building a non-capitalistic economic body with a free market; and a model of capital accumulation able to stimulate entrepreneurship, and to achieve the aggregate accumulation rate—a rate to be set by the community, with a view to eliminating

the tumorous growth of overheard and interest charges and the volatile disasters of finance capital.

The final section on the international market and disequilibria, wrought by the devilries of international finance, is but a beckoning call to drift toward a different conception of market economics, and a simpler and more transparent financial system than the dominant one, which is largely ridden by speculation, the concentration of power and the exploitation of the weak.

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## Coalition Governments: Fiscal Implication for the Indian Economy

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### Abstract

*The Indian polity has been through 43 coalition governments at the state level between 1966/67 and 1998/99. In the present study we attempt to examine what this change in form of government from single party to coalitions has meant for the economy. The results of our study which examines the post 1980 period give us reason to be optimistic. Coalitions at the state government level appear to have, on an average, done well to increase capital expenditures particularly capital expenditures on social services and other developmental categories. They have, however, not succeeded in taking politically hard decisions of curbing revenue expenditures and revenue deficits. It is our contention that the weak majority of coalition governments is their major strength. The tenuous hold of coalitions on power gives them a license for undertaking reforms. If the opportunity is taken to undertake the more 'politically difficult' reforms to prune revenue expenditures then the 'era of coalitions' would turn out to be a blessing in disguise for the Indian economy.*

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