Across the crises of modern capitalism

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Abstract

This essay provides a preliminary assessment of the transition from the 1929 crisis (and its solution) to the 2008 crisis. It points out how the modalities of the solution of the first crisis have paved the way for the recent crisis. The paper hangs the description and explanation of the whole process on a combination of the notions of business cycles and phases of development, a combination that allows the representation and explanation of the successive and various patterns of capitalism across the considered historical period. Thereafter we underline, mainly using the notion of functional imperatives, the important institutional transformations required in the passage from one type of capitalism to another, and the destabilizing effects that have resulted from the absence of those transformations in the wake of the emergence of conflictual-consumeristic capitalism and financial capitalism. On this analytical basis, we ground the widening of the recent crisis, showing a growing menace of long-term stagnation, contradictions and conflicts. Finally, the paper delineates some institutional reforms essential to overcoming the structural deficiencies inherited by conflictual-consumeristic capitalism and the dawning and no less damaging drawbacks that are being prepared by financial capitalism.

Keywords: Business cycles; Phases of development; The present failure of demand models; The question of money; Oganization of financial markets; Separation principle

1. Introduction

The topic of the conference requires an analysis of the character and the content of the three phases of the capitalist mode of production that have followed competitive capitalism, namely: monopoly capitalism, conflictual-consumeristic capitalism, and the financial capitalism now at work on a world scale. The absence of such an analysis is liable to generate great misunderstanding with regard both to the diagnosis of the considered crises and the suggested therapies.

Monopoly capitalism, an outcome of the second industrial revolution, is associated with high increases in labour productivity. Yet the competitive character of the labour market kept down the level of wages. This lowered the degree of absorption of production through consumption, at the same time causing a high increase of profits; while investment, due to the psychological volatility of entrepreneurs' expectations, was unable to account for the absorption of profits and, more generally, the level of production exceeding consumption. The consequent deficiency of effective demand, and hence unsold production, caused the reduction of output and the growth of unemployment, therefore a further and cumulative fall of demand that pushed towards the great economic crisis of the thirties.

J. M. Keynes clearly understood – in stark contrast to the dominant economic thought of his day – the demand led nature of the crisis. He suggested appropriate remedies, mainly public expenditure, even if wasteful, and deficit spending (for the joy of politicians) and the construction of the welfare state. The substantial recovery that followed fueled a great expansion and opened the door to the advent of a new and completely different age: conflictual-consumeristic capitalism. The associated growth of wages and public deficit stimulated by deficit spending policies, resulted in an apparent excess of global demand, thus suggesting restrictive policies. But the absence of policies appropriate to the new structural deficiencies of the economy engendered stagnation.

Later, the growing power of financial capital and institutions, in the context of the globalization process, opened the door to the present age of financial capitalism, and to the large scale crisis presently upon us, which is far from being adequately understood and threatens to condemn the modern world to a structural and endemic state of depression.

The analysis of the considered events will bring us to consider the controversy on the demand pull or cost push nature of inflation. We make evident the growing inappropriateness of both these theoretical positions and try to delineate a more adequate explanation of the character both of inflation and the present deflation. The analysis will be accompanied by a discussion on the role of money, starting from the long and bitter controversy that grew up between the Keynesian theory stating that, by way of liquidity preference, the quantity of money determines the interest rate, and the orthodox monetary theory revived by M. Friedman and stating that the quantity of money determines the general price level. We clarify a different role plaid by money, in line with the character of conflictual-consumeristic capitalism, and make evident the misleading theoretical and practical implications of the above controversy.

This opens the door to a discussion on the financial system and its reformation: a simple and clear proposal aimed at erasing the troubles caused by the hegemony of financial system and to reduce this to its natural status of servant, instead of master, of production; we underline that this is an indispensable condition for surmounting many distortions afflicting the present age of financial capitalism.

Moreover, I provide the exposition of an important and I think ineluctable reformation of economic process, a reform based on what I call 'separation principle' and regarding the relation between the side of production and that of distribution of income, a separation able to allow full employment, social justice and the maximum possible degree of efficiency, and to overcome the endemic state of crisis, heavy contradictions, useless conflicts and the consequent growing degree of malaise.

2. Cycles and phases of development

The deepening of the two large crises that are the object of this conference, their differences and similarities, requires a preliminary analysis of cycles. More generally, an analysis of the course of human societies, their motion and transformation, falls and resurrections, is needed for understanding the institutional and ethical changes indispensable to the coming economic and social world. Of course, such an analysis should exclude some common notions of cycles that do not properly express cyclical motion, for instance, the so-called life-cycle of man or of a product. These supposed cycles only describe parabolic curves: birth, childhood, youth, maturity, old age, death; or, for new products: appearance on the market, diffusion, maturity, decay and possible elimination by the advent of new rival products. Such parables, which, moreover, may be cut short by untimely death or the rapid advent of new rival goods, do not express a cyclical vicissitude. In fact, cycles place side by side a succession of rises, decays and recoveries. As such, a cycle cannot be referred to individuals or specific goods but only to social systems. There is more.

Cyclical motion appears only in quite advanced economic and social systems, that is, societies endowed with institutions, ethical conditions and, in sum, forms of civilization that favor evolutionary motion. Various primitive societies have survived in stationary conditions down to the present age. The history of human societies has known great spurts of creativity followed by: (a) ruinous crises and disintegration, as is typical of pluralist, decentralized orders agitated by strong antagonism and competition but lacking organizational strength (ancient Greece being a case in point); or (b) an almost unbroken continuity of behavior across centuries, an interminable quasi-stationariness after having reached considerable levels of social and cultural development (this case is represented by the great centralized bureaucratic orders and empires, the most typical of which is the ancient Chinese empire). Both these kinds of social orders have known important periods of growth, have been hit and sometimes annihilated by natural disasters, military invasions or internal contradictions; thereafter, their cultural, ideological and social conquests have been partially revived and improved centuries later by other, ascending peoples.

Social processes have assumed cyclical contents only after the birth, in Western European countries, of the modern dynamic society; itself a consequence of the installation of the economy, with its mercantile and entrepreneurial action, at center stage and as the leading sector of the social system. Therefore, only by starting from such a transformation can the study of the motion of the economy and society benefit from the theory of cycles.

But the mere analysis of cycles is insufficient for the understanding of social processes. Such understanding, and the related comparison of different and subsequent cycles, requires a more general notion on which to graft cycles, namely: the notion of historical phases. Such a grafting is indispensable in order to understand the character and changeable content of the cyclical motion over time and, more generally, to arrange the process of becoming of human societies, that is, from where we come and towards where we are going: a grafting crucial, among other things, for making a comparison between the two large scale crises of 1929 and 2008.

The problem is how to identify in a scientific way the various historical phases. Identification can be based on the character of the general conditions of development in the course of history and, more precisely, on the institutional and ethical-ideological and organizational forms at large that must be fulfilled for reasons of organizational rationality and efficiency in the presence of the given conditions of development. We denominate those necessary organizational forms 'functional imperatives'; while we denominate 'ontological imperatives' the institutional and ethical forms able to feed human evolutionary skills[1]. So, the functional imperatives signal the historical phase of development, while ontological imperatives feed, with the dynamical capacities of social systems, the possible succession of phases of development. Let's insist that functional imperatives concern institutional, ethical and power forms required by the existing as well as the future phases of development; this allows us to arrive at important knowledge on the contents of coming ages.

The advent of dynamic society has entailed, not only the birth of the cycle of economic and social processes, but also the shortening of historical ages, as a consequence of the acceleration of the change of the general conditions of development. Our combination of the notions of cycle and phase of development uses a peculiar theory and explanation of the cycle, which is almost entirely ignored by the numerous theoretical studies of the cycle, such as those founded on: monetary causes, the behavior of the banking system and its instability and attitude with regard to interest rates; variations of stocks; interaction between the multiplier and the accelerator; the existence of ceilings and floors, etc. The cycle on which we insist results from the phenomenon of dynamic competition as expressing the interaction between entrepreneurship, innovation and uncertainty. Therefore, it is strictly endogenous in nature and, moreover, more inclusive than other cycles emphasizing innovation and entrepreneurship, such as the Schumpeterian ones. It is activated by entrepreneurs' actions, precisely, the entrepreneurial search for profit opportunities through innovation that causes disequilibria and uncertainty followed by arbitrage directed to derive profits from disequilibria thus causing the reduction of disequilibria and radical uncertainty and hence the advent of a new surge of innovations. So, uncertainty plays an important role in the whole process and is not merely intended as a cloud of unknowing but displays an endogenous character. This cycle can concern both the medium range (intermediate cycles) and the long run (long waves), depending on the character (radical or incremental) of innovations.

[1] See A. Fusari, 'Methodological misconceptions in the social sciences', Springer 2014, chapter 2

The cycle that shapes the dynamic competition process has deeply characterized, with a variable content, the history of the modern world, starting from the achievement by the economy of a leading role in medieval society. This opened the flood gates to the great creative and turbulent surge expressed by the Renaissance, which was followed by the tremendous wars and malaise that afflicted the seventeenth century (the 'iron century'). An age of relative and peaceful serenity cheered the eighteenth century and prepared the advent of the first industrial revolution, which was followed by a succession of capitalist cycles and phases of development, in particular four frequently cited long waves activated by very important innovations, and a fifth wave now in course, probably more intriguing, full of surprises and more demanding than previous ones.

In order to understand the two large crises of 1929 and 2008 and the associated cycles, it is necessary to start from the phase of monopolistic capitalism and follow with the two more recent phases and long waves.

3. The 1929 crisis and its solution, the appearance of new misunderstandings and contradictions.

3.1 The characteristics of the large-scale crisis of 1929 are well known. A large number of studies have generated a convergence of opinions on the nature of the crisis and the therapies that might have been used to treat it. Therefore, we limit ourselves here to a mere synthetic overview of the subject. Indeed, we shall concentrate our main attention on what followed the solution of the crisis: the implications of that solution and subsequent development of debate up to the 2008 crisis. Furthermore, we shall attempt to consider what will probable now happen.

Starting from the beginning of the nineteenth century, capitalism (in its so-called competitive character) experienced the advent of a fully dynamic competition. The instability of the economy grew with the intensification of this kind of competition, centered as it was on the interaction between entrepreneurship, innovation and radical uncertainty.

The intensification of innovative processes stimulates radical uncertainty, and this causes instability. The degree of such endogenous instability generated by the economic system largely depends on the share of saving of the national product waiting to be invested. In fact, and as is well known, investment concerns the long run and, therefore, is strongly influenced by changing expectations and, hence, by the level of uncertainty, which negatively influences expectations.

With the advent of so-called monopolistic capitalism, mainly as a result of the great innovations (steel, chemistry, electricity, petroleum and the internal combustion engine) that distinguish the second industrial revolution, the instability of the economy jumped again. Put precisely, profits grew substantially, due to the great increase of labor productivity and the contemporary weakness or inexistence of trade unions – or, in other words, the competitive character of the labour market in the presence of a substantial excess of labour force, which kept wages low; but the utilization of these high profits was made difficult by the instability of investment, which in turn caused an acute deficiency of aggregate demand and a strong fall of production and employment: the large-scale crisis of 1929.

The economic thought of the time, deeply influenced by (so-called) Say's law that production generates the demand necessary to absorb it, was unable to understand the new disconcerting situation, and was hence unable to offer analyses suitable for a solution to the crisis. A great confusion dominated the scene, both among theorists and practical men.

J. M. Keynes was the economist who properly diagnosed the nature of the crisis and the way to overcome it. He saw clearly that the crisis was a result of a marked deficiency of demand, and he saw too the causes of this deficiency. *Keynes' analysis provides an outstanding example of the unification of economics and political economy; in fact, his diagnosis implies the requisite therapies for the overcoming of the crisis*. He recommended the pursuit of full employment through the support of demand, based mainly on the incomes of the poor men (who have a high propensity to consume), deficit spending and the construction of a welfare state that has come to constitute one of the main achievements of civilization. As a result, Western nations came to know an age of progress such as the world had never known: a real golden age of capitalism that continued for more than twenty years and has transmitted an important inheritance to future generations.

A particularly important element of the new experience, however, was no doubt the advent of new contradictions, which were unfortunately ignored, as too were the transformations that they called for. This is what we have to examine, in order to be able to understand the roots of the increasingly serious difficulties and misconceptions that have led up to and followed the recent large-scale crisis of 2008.

According to Keynesian's teaching, investment is the instrumental variable *par excellence*: a variable which is not conditioned by the level of saving since investment would determines the saving it needs. This interpretation depends on the hypothesis that, in principle, capitalists' decisions on investment and consumption have an exogenous character and are the fundamental a priori element in the whole process.[2] But such a hypothesis is valid only in particular conditions. It was valid in the situation that Kaynes considered; but it is far from being valid in every case. In particular, the validity of the above hypothesis and perspective is strictly conditional on the collateral effectiveness of the Keynesian hypothesis that *trade union bargaining is able to determine only money wages but not real wages.* If this is indeed the case, then the distribution of income between wages and profits is forced to adjust (by definition) to demand, thus constituting a merely residual variable (i.e. a variable consequent with respect to the level and composition of demand, mainly with respect to the level of investment). This hypothesis entails that it is sufficient to influence demand and its composition in order to influence not only production but also (due to the consequent movements of prices) the shares of income distribution. In brief, the amount of profit depends on the amount of investment, what generates the saving necessary to finance investment and the same incentive to invest. Consequently, given the conditions postulated above, the problem of demand and capitalists' decisions on the amount of consumption and investment constitute the fundamental a priori of the whole process (demand led approach).

3.2 It is useful to repeat that *the whole approach is based on Keynes' hypothesis about the labour market; a hypothesis assuming that real wage has a residual character (inside the limits clarified by Kaldor, or within the limits of Robinson's 'inflationary barrier'). We label such an assumption the 'postulate of the residuality of real wages'*.

Now we must ask ourselves what are the indispensable conditions if the above postulate is to be made effective. It is clearly evident that the effectiveness requires at least one of the following conditions:

a) Workers are completely affected by the so called 'monetary illusion'.
b) The productive system is coming to the end of a period of chronic stagnation and entering into a new phase of great dynamism characterized by a high rate of development or a strong 'acceleration' of the growth rate. In these conditions, the capacity of capital to pay wages can even precede as well as fully meet wage claims, thereby avoiding a real conflict over income distribution.
c) Workers' contractual power is very weak so that they are forced to submit to the bargaining power of the opposing party. Such weakness cannot be attributed to a supposed almost unconditional control of capitalist, and the ready availability, of financial resources.[3] In fact,

[2] The same hypothesis characterizes Kaldor's approach. Kaldor introduces into the model the natural rate of development and hence technical progress and demographic increase; nevertheless, he attributes to investment the role of substantial and main instrumental variable.

[3] Kregel wrongly emphasizes this aspect. He writes: "The possibility of creating financial means previously… with respect to effective production… allows entrepreneurs to owe real resources according to their real earnings and their wealth… The possibility for capitalists to dispose some financial resources in order to buy resources to be invested confers on them the control of last instance of the proportions according to which the available resources by the system take the form of consumption and investment" and hence (we may add) of wages and profits. See J. A. Kregel (1975), p. 225.

this does not imply an unconditional control of the labour force, even if it constitutes an indispensable premise for such control. This control requires indeed much more: substantially, in market economies, it requires the operation, in the presence of an adequate excess of labour force, of both the mechanism of demand and supply of labour and the collateral absence of the indexation of wages (or the absence of trade unions with sufficiently strong bargaining power) so as not to allow them an almost complete covering of inflation.[4]

It is easy to see that condition (a) can only work for brief intervals of time and only occasionally, unless the working class is particularly ingenuous. The same is valid for the situation under (b), which after all does not represent a Keynesian condition of stagnation of demand, even if it is consistent with the Keynesian view intended in a more general sense. In sum, the effectiveness of the Keynesian postulate of residuality of real wages requires the situation under (c), that is, that wages depend on the availability of labour force in the presence of large scale unemployment.[5] This was the situation that Keynes actually observed and that enabled him to presume a substantial residuality of real wages and, consequently, to ignore the problem of income distribution or to consider it as a consequential and secondary issue, without thereby violating reality but perfectly interpreting its contents.

Later N. Kaldor and J. Robinson (who lived in a period increasingly concerned with the problem of income distribution) subjected the above postulate of residuality to the constraint that real wages exceed the subsistence level. Such a correction does not undermine the substance of the considered theory;[6] but it is far from being satisfactory when (as we shall see) it comes to the interpretation of a world in which the operation of the condition of the demand and supply of labour force is increasingly and explicitly contradicted by observable facts.

Moreover, it must be reminded that Kaldor and Robinson's theory of income distribution,[7] as also Pasinetti's contribution on this subject,[8] suppose the full employment of resources. This hypothesis enables these three economists to provide a rigorous definition of the shares of income distribution. But their analysis concerns the long run and assumes that any situation of deficient demand has already been remedied (through Keynesian therapies). This *Cambridge* theory of income distribution, founded on the postulate of residuality of real wages*, implies an a priori denial (through the hypothesis of full employment) of the possibility that two of the above conditions (required by that postulate) are verified.* These conditions are (b), concerning the short run, and (c), that is, the operation in the labor market of the mechanism of demand and supply of labour, in the presence of an excess of labour force, etc. Therefore, the postulate at the basis of the post-Keynesian Cambridge theory of distribution could operate only if condition (a) – concerning monetary illusion – is also operating. But unfortunately this possibility is completely unrealistic with regard to the long run. *So we must conclude that the Cambridge theory of income distribution is contradictory, being based on contradictory assumptions (full employment in a long run perspective and residuality of real wages)*.[9]

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[4] It is not necessary that this covering is total. In fact, if the covering of inflation through the indexation of wages is near to one, a very high rate of inflation would be necessary to allow the profit share to rise.

[5] This means that, in practice, the statement that wage bargaining is in terms of money wages but not real wages does not imply that labor market conditions do not influence real wages. In fact, the independence of real wages from the contents and the results of wage bargaining depends, after all, on the particular conditions of the labour market that Keynesian theory implicitly presumes, unless the situations under (a) and (b) are verified. This is possible with reference to the short run. In fact, in this case the postulate of residuality of real wages is operative also in the absence of condition (c).

[6] Kaldor himself underlines that subsistence wages only characterize the initial stages of development. See N. Kaldor (1965).

[7] See J. Robinson (1961).

[8] The main contribution of Pasinetti in this regard is his article entitled 'Rate of profit and income distribution in relation to the rate of economic growth'. *Review of Economic Studies*, vol. XXIX, October 1962.

Of course, the Cambridge theory has some other problem as well, for instance, Kaldor's mechanism through which full employment equilibrium is achieved, or the a priori assumption of Robinson and Pasinetti as to the existence of such equilibrium.[10] But, in contrast to the analysis above, these are issues that do not concern the foundations of the theory under consideration.

4 Consequences and meaning, for demand led models, of the non-operation of the postulate of residuality of real wages

The success of Keynesian recipes opened the door to a new and – in terms of content – opposite phase of development with respect to monopolist capitalism, which can be denominated *conflictual-consumeristic capitalism*. This new state of affairs was characterized by competition based largely on new products, the stimulation of consumption through advertisement, high wages in the most dynamic sectors, due to both the increased bargaining power of trade unions and to the interest of firms in stimulating the consumption of new goods and maintaining an unvaried mark-up margin so as to obstruct the entrance of competitors, as well as to avoid loss of profits due to strikes. This is a quite different world to that expressed by the phase of monopolistic capitalism, which latter excluded the relevance, in conflicting terms, of income distribution, even if it emphasized the contribution of this to demand.

In the case that the postulate of residuality of real wages does not work (*that is, that the hypotheses set out in sub-section 3.2 of the previous section are erased by conflictual consumerism*), the advent of pressures on the side of distribution will imply that profits come before investment; *in fact, in this case the decisions to invest are conditioned by their profitability, not vice versa.* This means that, in the presence of the condition here supposed, interventions on demand cannot remedy the difficulties at work (on the contrary, they may worsen them, as in this condition the distributive shares cannot simply adjust to the level and composition of demand but rather follow a logic that leaves out of consideration the shape that demand will assume and is anterior to this shape). It is important to consider this point in some detail.

Let us make the assumption that, due to the class struggle and in the absence of the operation of the postulate of residuality of real wages, profits fall too low. In these conditions, investment decreases (for various reasons: both due to financing, because entrepreneurs thereby hope to determine a change of distribution to their own advantage, and because profits are the main stimulus to entrepreneurship). With the decrease in investment comes also a parallel decrease of production or, in other words, *a decrease in the degree of utilization of the available resources.* At the same time, the increase in the labour share of income accompanying the above circumstance will cause a collateral increase in the share of consumption of total income. Probably the public deficit will also grow as a consequence of the intermediary role that public administration fulfils in the struggle for income distribution, especially if this struggle is particularly harsh. In the presence of these conditions, analysis will reveal, on the whole, quite a high level of demand (notwithstanding the reduction of investment and the under-utilization of productive capacity). This high demand is due to the expansion of consumption and, probably, also of the amount of the public deficit.[11] (We shall see later that, in the presence of these conditions, the demand for goods and services, with respect to their production, will be remarkable in the average). Therefore, *such analysis will inform us that we are not in the presence of a deficiency of effective demand but rather in the presence of a problem*

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[9] It could be objected that the assumption of the full utilization of capital (but not labour) would make valid the post-Keynesian theory of income distribution. But such a hypothesis (scarcity of capital with respect to labour) can be considered appropriate only with reference to underdeveloped economies, for which the Keynesian theory is not valid for different reasons, that is, due to the absence of homogeneity of the economic system, indispensable to make effective the leadership of demand.

[10] In this matter, it may be useful to refer to an article by U. Marani (1976).

[11] It may be useful to underline that while a deficiency of demand can happen in this case, it can arise as a consequence of restrictive policies directed to reduce the inflationary pushes due to pressures on distribution (which last remains therefore the fundamental a priori element of the situation).

concerning the composition of demand; specifically, this is a problem arising from the unsatisfactory level of one part of demand, namely, investment. As a consequence, the increase of some other component of demand will not improve the performance of the economy (as, on the contrary, would happen in Keynesian conditions).

It may be objected that the under-utilization of plant is an obstacle to investment and that the expansion of demand constitutes, therefore, in this case, an incentive to investment. But only the premise of the above objection is correct; *the deduction is a great and very frequent error*. Such a deduction would be right only on the hypothesis that the problem starts from the side of demand, and is clearly incorrect if it originates in distribution (and when the squeeze of demand, if present, is only consequent to restrictive measures directed to control inflationary pushes caused by pressure on distribution).

Moreover, a careful analysis of the condition of demand will inform us that not even a policy of direct support of investment (this representing, in the supposed condition, the weakest component of demand) may remedy the situation. Let's set out the reason for this.

4.2 The situation can be characterized (again) in terms of an ex ante excess of saving with respect to ex ante investment, arising from the fall of investment. But investment does not represent, in the postulated conditions, the instrumental variable *par excellence,* as it does in Keynesian schemes; in fact, investment cannot be freely stimulated. More precisely, it cannot be presumed that an adequate increase of this variable is able to return the economy to motion and warrant an adequate profitability. Of course, it is in principle possible to increase public investment, that is, the exogenous part of investment. But this will not of itself cause an automatic increase in the performance of private investments and, hence, will not cause their increase (as would occur if the postulate of residuality of real wages were working). Therefore, private investment will continue to stagnate, due to its supposed low profitability. Moreover, from the fact that in the postulated conditions investment is in itself unable to generate profit, it can be inferred that this investment has not the thaumaturgic virtue of generating the saving that it needs. This implies that an increase of the public deficit aimed at financing exogenous (public) investment, instead of contributing to the stimulation of production, can further worsen the performance of the economy and simply subtract resources from private investment. The accumulation process would be stimulated only if, collaterally to the increase of exogenous investment, some decrease of consumption and public deficit and adequate transfers (mainly in the form of incentives) to firms were in operation. But such a policy is quite different from the mere stimulus of demand. Moreover, while this should provide a stimulus to the accumulation process, it will not warrant its continuation.

For the sake of maximum clarity, these considerations on investment can be put in a different and more general form. In demand led models, the fall of investment is generated by the volatility of expectations. As is well known, the rise of demand makes expectations more optimistic, thus stimulating investment and hence determining an expansionary spiral. However, if the fall of investment is due to distribution pressures that reduce profit (a situation less volatile than that in which expectations play the major role), the stimulus of demand is unable to stimulate investment and production. For in this case it is the struggle for income distribution that is the starting point of depression, and the rise of demand is impotent with regard to making the terms of this struggle more favorable to capital; indeed, if anything, the opposite is likely to occur.

4.3 In an open economy, the operation of the postulate of residuality of real wages is also obstructed by the fact that any increase of the prices of commodities produced by domestic entrepreneurs is opposed by the competition of foreign goods, both abroad and in the domestic market. Therefore, in this case, the conditioning arising from the side of distribution is more stringent and may cause an increase of imports, a decrease of exports, and even an increase in the export of capital for reasons of profitability, thus worsening the deficit of foreign accounts. This will cause a squeeze of demand directed at reducing such a deficit. In sum, it should be clear that, in the conditions described above, the squeeze of demand is generated by a situation that genetically has little to do with the level of demand. Of course, the situation described will be considerably exacerbated by any increases in the price of imported raw materials.

So, the struggle for income distribution, which is an important component of modern societies starting from the advent of conflictual-consumeristic capitalism, generates some apparent conditions of deficiency of demand that may, in turn, give rise to mistaken interpretations as to the behavior of the economy and, consequently, the suggestion of erroneous therapies. It is therefore important to set out some other clarifications on the matter.

4.4 The operation of pressures on the side of income distribution causes inflation. This implies that the previous analysis allows also for some clarification regarding inflation.

The debate on the nature and causes of the increase of prices has always been fierce. It gave rise to the well known controversy between Keynesian and monetarist approaches. The monetarist theories will be considered in the next section.

Keynesian economists do not have a univocal position on inflation. The main bone of contention concerns whether the primary cause of inflation lies in demand-pull or cost-push.[12] We hope that our analysis is able to provide some clarification of the controversy. *The Keynesian arguments surrounding inflation arise due to a pretense that much more can be extracted from the Keynesian approach than it is actually able to say.* But the controversy over cost-push and demand-pull causes of inflation cannot be resolved within the Keynesian approach and, indeed, the arguments become circular, resulting in profound misunderstandings. However, if abandoning those schemes, we approach the analysis of inflation through a more global and less unilateral approach we can hope to obtain a useful clarification on the controversy. This point can best understood in light of our previous discussion, as we shall now see.

So-called cost-push inflation increasingly appears to be due to pressures arising from conflict over the distribution of income;[13] such pressures constitute at present the single most important cause of inflation. We have seen that these pressures come together with a substantial expansion of public expenditure (due to the intermediary role that the public administration is obliged to perform in the presence of marked social conflict) and, more generally, with an excess of demand (intended as discussed in the previous point above). This conflation gives to those inflationary motions the appearance of an inflation stimulated by demand; thus providing one part of the Keynesian economists seemingly good reasons for maintaining that this is in fact the case.

But we know that the pressures surrounding income distribution are also accompanied by some degree of under-utilization of resources, thus enabling other Keynesian economists, who see in this under-utilization of resources a clear indication of the deficiency of demand, to maintain that inflation is due to costs. But the indication of this under-utilization of productive capacity as a proof of deficiency of demand is senseless, as we know. These latter economists could properly defend the thesis that the inflation is due to costs only by abandoning the Keynesian scheme.[14] And in fact, as soon as we do abandon such an approach, the equivocation disappears: it *becomes clearly evident that it is completely mistaken to consider this inflationary motion as due to demand and*

[12] On such controversy and the attempts to resolve it see, in particular, the articles by: S. Weintraub (1980), and R. J. Bole and R. S. Bodkin (1972).

[13] Inflation due to the costs of imported raw materials should also be considered as a consequence of pressures concerning the distribution of income or, more precisely, as a consequence of the redistribution of those costs among various countries. More generally, the cost increases of raw materials must be considered primarily as a consequence of the international conflict for the distribution of wealth among developed and underdeveloped countries.

[14] *Cost inflation would be consistent with the Keynesian scheme only if the entrepreneur were able to answer the motion of money wages with collateral increases of the prices of produced goods able to neutralize the pressure of this motion on income distribution. In fact, in this case the postulate of residuality of real wages would operate*. But this could happen only on the extremely unrealistic hypothesis that workers are plainly subject to monetary illusion and international competition is absent. In the absence of these conditions, the above motion of wages would cause considerable pressures on income distribution and this *would force the analysis outside the Keynesian approach.*

operate interventions based on such a conviction. At the same time, we perceive the substantial appropriateness of the alternative point of view.

But we consider it more appropriate to indicate the inflationary motion considered here as an inflation due to distribution, in order to capture the real nature of the inflation; and I dearly hope that such reflection throws some light on a controversy that, if not solved, will continue to generate profound theoretical and empirical misunderstanding. The next section will provide a more complete treatment of the matter.

5. A brief review on the role and operation of money from the thirties of the last century to the present time

Both the role and the meaning of money have changed substantially over time, in parallel with some important transformations within the economic and social systems. We have seen that the period between the second and third industrial revolutions witnessed the diffusion of oligopolies together with a related large increase in productivity, low wages and variable entrepreneurial expectations and investment, and hence a recurrent deficiency of effective demand and increase in liquid money. The emergent situation persuaded Keynes to emphasize the idea of liquidity preference and to base the explanation of the rate of interest on the supply and demand for money, as opposed to the earlier appeal to the quantity theory of money and related account of the interest rate in terms of the relationship of savings and investment.[15] But as is not infrequent in the history of social thought, the Keynesian view triumphed only at the moment when its own foundations began to be shaken by further social and economic development.

From the seventh decade of the last century, a long and bitter controversy grew up between the Keynesian theory that (by way of liquidity preference) the quantity of money determines the interest rate, and the orthodox theory revived by Milton Friedman that the quantity of money determines the general price level. Actually, late twentieth-century socio-economic conditions fitted neither monetarist nor Keynesian theories. Precisely, the late second half of the last century witnessed a fundamental and unprecedented change, a transition from monopoly capitalism to what we have called conflictual-consumeristic capitalism (that, as we saw, was distinguished by: advertising mainly directed to stimulate consumption of new products; high wage increases in advanced sectors stimulated more by the firms' interest in stimulating the demand of new products and keep mark-up unvaried, than by trade unions demand; imitational growth of wages and consumption in the less dynamic sectors of the economy). One consequence of this transformation has been a qualitative change in the role of money, which may primarily be expressed as the increasing importance of what may be called the 'nominal demand for money', *i.e. variations in the quantity of money have been endogenously stimulated, and this by both price changes and in consequence of the conflict for income distribution*[16]. This demand for money is just the opposite of the Keynesian preference for liquidity associated with the deficiency (or excess) of effective demand. In fact, while the notion of demand for real money (liquidity preference) refers to the role of money as a fund of value, the demand for nominal money concerns the role of money as means of payment. More in general, this new situation, characterized as it was by the *endogenous* supply of money, differed substantially, both from the situation diagnosed by Keynes,[17] in which exogenous variations of the money supply

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[15] Hobson's study on imperialism preceded Keynes in underlining the explanatory role of the deficiency of effective demand, but his analysis disregarded the question of money and interest rate.

[16] See A. Fusari (1981)

[17] Some neo-Keynesians, e.g. N. Kaldor and J. Robinson, underlined the endogenous character of money variations. But they did not consider that this endogenous character destroys the relation between the money supply and production based on the interest rate; in fact, they ignored its reductive impact on the preference for liquidity and hence on the validity of the theory of interest rate based on the demand and supply of money. These students did indeed express doubts on the incisiveness of the relation between money supply and production, but for different reasons from those we underline, and they sometimes improperly assimilate interest rate to profit rate.

determine the interest rate, and from the situation described by the quantity theory of money, according to which exogenous variations of the money supply determine prices.

So, the Keynesian doctrines were not equipped to react to (and govern) this consumeristic landing. Their foundation on demand induced consideration of the new situation as characterized by an excess (rather than a deficiency) of effective demand, thus suggesting the necessity of reducing such an excess through restrictive monetary policies (that is, the contrary of the expansive policies required in the presence of a deficiency of effective demand). This condemned consumeristic capitalism to the phenomenon of *stop-go* and the distinction between short and long period problems, with the short run problems prevailing as more imperative over the medium and longer period structural issues constituting the back bone of programmatic designs. Precisely, structural policies were systematically postponed in the name of short run exigencies, putting off their application until the advent of better conditions that, in the absence of any solution to the structural deficiencies, never arrived. The dominant economic thought of the day was not equipped to allow understanding that the new phase had nothing to do with the traditional theories of money, be they Keynesian or quantitative. So, Keynesianism was now caught out of time; a situation that facilitated the monetarist reaction. What is worse, the old Keynesianism blocked understanding that structural action and reformation was indispensable even with regard to the control of short period depression by way of the elimination of the decay and dead ends caused by conflictual-consumeristic capitalism.

Let us examine more closely the substance and the effects of this new state of affairs. Inconvertible paper money constitutes an efficacious instrument for taking the sting out of some of the contradictions that may afflict the economy. In particular, it has the potential to diffuse the impact of the conflict over income distribution upon weak and/or ingenuous social groups. Employing a literary parallel, we may say that inconvertible money resembles don Circostanza (don Circumstance), an intriguer and opportunist lawyer, who in defense of the people of Fontamara[18] against the plan of the mayor to deprive them of the water of the brook, proposes that each of the two conflicting parties be awarded ¾ of the water. With this trick, he succeeds in placating a protest of the people intended to preserve more than one half of the available water.

In conflictual-consumeristic capitalism, the money supply is stimulated, as just seen, by endogenous factors, primarily the conflict over income distribution. In some sense it reproduces don Circostanza's expedient to placate Fontamara's conflict by promising to the opposing parties more than the available water. In the presence of money illusion, a modest inflation is sufficient to make don Circostanza's strategy bear fruit. But what happens if people begin to detect the illusory quality of money wages and the object of the bargain becomes real wages? The expansion of public expenditure and public debt may become an alternative path to the elimination of the difficulties and inconsistencies that arise out of the struggle for income distribution. But it is only an apparent alternative. In the end, the financing of the public deficit stimulates the 'nominal demand for money' (the endogenous character of the last), and hence inflation.

It is precisely this 'cheeky' use of money that has opened the door to some of the main difficulties afflicting financial markets today.

6. What about the present?

The behaviors referred to above drive (and force) the progressive restoration of the exogenous role of money; a restoration, however, that may be undermined by a heavy inheritance of public debt and inflationary potential. The situation is aggravated by the operation and strength of international financial markets in the modern global world, where speculation shifts enormous masses of capital instantaneously. There is no supranational authority able to discipline these activities and prevent

[18] See Ignazio Silone (1990 [1930]).

the crises provoked by massive transfers of hot money.[19] The evolution of financial instruments and markets easily renders obsolete older guidelines and codes of conduct. Worldwide speculation may force monetary depreciation upon monetary authorities, resulting in inflation and a perverse impact on financial markets. In this state of affairs, the restoration of an exogenous money supply becomes a difficult, not to say impossible task, while the control of the financial market is no longer within the hands of the individual sovereign state. A new age or phase of development has started: *financial capitalism*

The interest of students of economics in financial capital dates back more than a century. R. Hilferding's book, *Das Finanzkapital* (1910), captured a great deal of attention. But the dominant role, and hence the age, of *financial capitalism* began only recently, with the great acceleration of the globalization process on a world scale. The core of modern capitalism is finance and financial speculation. 'Production of commodities by means of commodities' has been substituted by the production of money by means of money. Enormous holdings entail a combined control of important banks, industrial and commercial firms, and strongly influence political power: an extremely fragile state of affairs notwithstanding appearances, which, moreover, strongly stimulates disequilibria and inequalities.

But the great holdings are a degenerate phenomenon that found on mere power relations both profitability and influence. From being a servant of production, financial capital has become master of production: a degenerate master, indeed, the agent of a truly unnatural transformation. The ghost of spread persecutes national states. The international financial market is submerged by financial by-products (hedge funds, private equities): a deceitful and extremely unstable house of cards.

At the present moment, the situation of the European Community appears to be particularly acute and confused in this regard: the restoration of the exogenous character of the money supply is obstructed by the absence of a sovereign monetary authority concerned with the new currency, the Euro. The result is an almost free terrain for international speculation that is primarily the consequence of the large economic and financial disequilibria existing between the various European economies, which condemns those countries afflicted by high public debt and some risk of insolvency both to high interest rates and to the enactment of significant reductions of public expenditure, wages and hence demand, with a consequent and endemic stagnation and a substantial inability to reduce public debt.

We have seen that some of the main problems that have entangled the role of money with the behavior of financial markets derives from the conflict over income distribution, the mediating role of public expenditure and the consequent variation of money supply following what we have called the 'demand for nominal money'. We have further seen that the attempt to control the consequent inflation has often initiated restrictive money policies, thus generating recession or, as an alternative, money devaluation, along with the inevitable implications for financial markets. We shall see in the final section that one way to avoid these drawbacks is the separation of income distribution from production, with the exception of material incentives required by particularly undesirable or risky activities, thereby reducing the market to a mere mechanism for the imputation of costs and efficiency and, in this way, preventing the conflict over the distribution of income from affecting the production side. This separation seems necessary in order to meet the disorder of financial markets previously outlined.

7. Basic organizational needs of the present and coming economic systems

Now we come to consider what suggestions may explain the combination of the cyclical motion, generated by dynamic competition, with the notion of phases of historical development (a combination discussed in section 2) mainly the requirements in terms of functional imperatives. As we have seen, the modern phases of development are shortened by the acceleration of evolutionary

[19] Significantly, J. E. Stiglitz (2002) has harshly criticized IMF policies.

processes under the pressure of dynamic competition. We are going to ascertain the 'necessity' of transition, along this road, towards something different from capitalism.

The acceleration of economic growth due to the first industrial revolution has opened the door to a succession of capitalist phases of development: competitive capitalism, monopolistic capitalism, conflictual-consumeristic capitalism, and, finally, financial capitalism. Four large crises and long waves have accompanied such succession, intermingled with intermediate and short cycles. What new institutional and ethical-ideological forms are required by these passages, in particular, that which is today in progress, 'financial capitalism'?

Two phases of development have been known by modern world after the triumph of Keynesian revolution: conflictual-consumeristic capitalism and financial capitalism. Unfortunately, the world is far from carrying out the basic functional imperatives (as considered in section 2) requested by the two phases and the corresponding general conditions of development. Only secondary and contradictory transformations have been performed, being transformations hindered or strongly conditioned by the capitalist character of the economy. The previous sections have tried to give a representation of this difficult process of rationalization. The difficulties probably are due, and they tend to grow, because the continuous process of change at work, inaugurated by the advent of capitalism, needs something not contemplated by capitalism.

We shall consider now two basic functional imperatives and reorganizations that are required by the phases of conflictual consumeristic capitalism and financial capitalism, starting from this second phase for reasons of continuity with the previous two sections.

7.1 A proposal concerning the organization of financial markets

We delineate here a blueprint for a financing system of production capable, among other things, of clipping the wings of financial capital, stimulating entrepreneurship and contrasting the deficiency of global demand, and achieving a far greater openness than exists at present toward social justice. The financial system at present is a very complicated and slippery beast; we have seen that it is also heavily subject to malfunctioning and the tricks of speculation. It seems to us that the financing of production does not need such a complicated and insidious system, and could largely be replaced by the operation of the banking system, albeit not in its habitual features.

A discussion of the procedures required to modify the banking system in accordance with what follows is not relevant in this context; a detailed analysis of the matter may form the theme of another paper. The important point that needs to be emphasized at this juncture is the need to radically modify the central function of the banking system with regard to the funding of production. Financial capital is not at present at the service of production but, for the most, it enslaves production and exploits the toiling community into the bargain. This distortion needs to be redressed in the sense that *financial institutions become the servant, not the master, of production.* Our proposal, aimed at heavily simplifying the complicated set of financial markets and activities, is presented here in as simple and transparent fashion 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 individual 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 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.[20] However, savers should not be allowed to buy shares directly, since

[20] A real interest rate of zero percent on saving would actually be a bargain for savers who, over 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 in financial markets. In another book by H. Ekstedt and A. Fusari entitled 'Economic

the stock exchange is much worse than a gambling house. The rest of the funds required to achieve the planned rate of accumulation will be provided by a Fund of Common Wealth (see sub-section 7.2 that follows). This fund should channel the necessary quota to the banking system, to be distributed among firms. The banking system should also finance investment abroad, mainly in underdeveloped countries.

Each bank's application to the fund for resources should be judged on the basis of its 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, thus 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 allow them to achieve the community's projected accumulation rate.* Therefore, if the banks' requests for capital do not exhaust the fund set aside for accumulation, the difference should be assigned compulsorily by the Fund of Common Wealth 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 the applicant firms' 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 lend funds up to the accumulation target. So banks are induced to make golden bridges to entrepreneurship.

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

The processes of globalization generate an increasing, and increasingly complicated role for the financial system in the contemporary world economy. By contrast, production, even if projected on a world scale, is subjected to largely national and local constraints. Moreover, production suffers from the clear – and yet often undecipherable - hegemony of the financial side. The financial system devised here should eliminate the complications, tricks and unconstrained speculations of current financial systems, with their worldwide power over production.

7.2 Production and distribution within the market operating as a pure mechanism of imputation of costs and efficiency

We delineate now another functional imperative, this time requested by the phase of conflictual-consumeristic capitalism, that is, to avoid the afflictions and contradictions that the advent of this

Theory and social change' (Routledge 2010), chapter 8 by A. Fusari, I have shown the exogenous nature of interest rate and the possibility to reduce to zero its rate expressed in real terms. It must be added that the zeroing of real interest rate is also important to avoid a main cause of growing inequalities in income distribution that Piketty 2014 underlines as consequent to the tendency of interest rate r to exceed the rate of growth g.

phase has implied, as discussed mainly in section 4. This functional imperative mainly consists in what we shall denominate 'separation principle' of income distribution from production, but not vice-versa.

We have seen in section 2 that the operation of dynamic competition, the basic feature of modern economies, is expressed by the interaction between entrepreneurship, innovation and uncertainty in the context of the market mechanism. Both in private and public companies (operating for the market), the only reliable indicator of success and hence of responsibility is the profit rate[21]. All other significant indices refer only to particular aspects of entrepreneurial action; they are partial and may accordingly become misleading.

We also know that the operation of dynamic competition has determined a succession of phases of development that tends to accelerate in the course of time, and that each one of those phases is distinguished by some new functional imperatives.

One main goal of our reformist proposal 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[22]. 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 relation 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 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. The first course of action is completely senseless in modern dynamic societies, while the second perspective appears nowadays utterly insufficient[23].

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, a Fund of Community Wealth that 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 proposal functions by starting with production.

In the proposed model of organization, 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 labour[24].

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[21] 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.

[22] 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.

[23] The debate on market socialism in the years between the two wars was hinged on the hypothesis of a stationary economy, which does not need entrepreneurship, and thus made room to the formulation both of a centralized model of the economy, as 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

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

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 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 Job Centers, 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 Job Centres 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[25]. The

expressed in money units.

25 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;

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 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[26]; 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.

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.*

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moreover, it makes the hypothesis that wage rate is exogenous, that disregards the relation between wage rate and the supply and demand of labour.

[26] M. Polanyi's pioneering insistence on *tacit knowledge* has provided a deep and extensive illustration of this aspect

Let me also point out that the idea of the workers' self-management[27] of the firm is mistaken. And the workers' remuneration based on firms' results is a vehicle of inequalities and managerial degeneracy. 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 farseeing 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 has been clarified in discussing how firms should be financed.

In conclusion, it should be clear that income distribution concerns the entire society and that even production is a social entity since it depends on productive forces engendered by society, such as techniques and knowledge. Some ingenuous 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

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

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.*

We call our approach a 'necessary' model. It also includes the costs of factors as determined by their availability, but just in the mere quality of production costs, that is, excluding any implications (except material incentives, as previously noted) on income distribution, this latter being the object of policy choices. For its part, the profit rate (intended separately from interest on capital) mainly plays an accountability role or, more explicitly, is primarily a measure of the degree of success of entrepreneurial actions and decisions, both in private and public firms. These features of our 'necessary' model and, in particular, the implied exogenous nature of income distribution, warrant the inference that the operation of the production side is only affected by the availability of resources (and, of course, by demand) and would allow the restoration of a genuinely exogenous role of money.

8. Conclusion

This essay has shown that the growing varieties of theories and visions characterizing economic thought is mainly due to some basic misunderstandings on the changeable economic and social reality, instead of being the expression of a sound and fecund pluralism. The misunderstandings darken, among other things, the meaning and the propulsive role of ideologies. In the absence of science, men have recourse to intuition and common sense. But this is not enough to face the growing change caused by the rapid development of knowledge on natural phenomena and technology.

The above cognitive penury has heavy consequences at world scale, the reduction of which needs a penetrating criticism of the economic system that dominates to day the international landscape.

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. Capitalism is not western inventiveness as a whole; it is but a proprietary scheme that has usurped 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 suffocation 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 overhead and interest charges and the volatile disasters of finance capital.

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