Corporatism and Keynes: His Views on Growth

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Of the main contests in 20th century political economy, the contest between capitalism and corporatism still matters. And it matters quite a lot, as I believe the recent economic record of continental western Europe helps to confirm.[1] My discussion here of the economic thought of John Maynard Keynes will focus on his early "corporatist" dissatisfaction with the market – a dissatisfaction that ran deeper than the Pigovian critique of *laissez faire,* later known as the "free market" system.

Intellectual Currents in Keynes's Day

Before we can discuss Keynes in relation to corporatism and capitalism we have to ask: What do they mean now? And in what ways did their meaning differ in Keynes's day?

Today, a predominantly capitalist economy, whatever its minor deviations from the ideal type, means a private-ownership system marked by great *openness* to the *new commercial ideas* and the *personal knowledge* of private entrepreneurs and, further, by great *pluralism* in the *private knowledge* and *idiosyncratic views* among the wealth-owners and financiers who select the ideas to which to provide capital and incentives for their development.[2]

A corporatist economy today is a private-ownership system with some contrasting features: It is pervaded with most or all of the economic institutions created or built up by the system called *corporatavismo* that arose in interwar Italy: big employer confederations, big labor unions and monopolistic banks – with a large state bureaucracy to monitor, intervene and mediate among them. Yet without some knowledge of the purposes for which the system was constructed it cannot be understood at all adequately.

I think it is fair to say that the core function of the distinctive corporatist institutions is to give voice and levers of power to a variety and range of social interests – "stakeholders" and the "social partners" in postwar terminology – so that they might be able to have a say or even a veto in market decisions that would harm them. The individualism of free enterprise is submerged in favor of these entities and the state

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1 Many blame the "social model" for the Continent's relatively high unemployment and anemic participation rates, though perhaps not for the lower hourly productivity. And, empirically, employment does not appear to have suffered in the U.K. and Ireland in spite of their large welfare outlays.

2 The term *free enterprise* might convey better this Hayekian conception of capitalism but I would rather not proliferate terminology.

representing them. This purpose, or function, expresses what might be called *solidarism/communitarianism* and *consensualism/unanimitarianism*. The very word "corporatism" (*corporatavismo* in Italian) derives from *corporazione*, the Italian word for the medieval gild, which served to empower the artisans in a craft.[3] It is clear on its face that the system operates to *facilitate* the introduction of changes in the direction of the economy sought by the state, following consultations and negotiations with stakeholders and social partners, and to *impede* (thus also to discourage) or *block* changes opposed by some of the stakeholders or partners: relocations of firms, entry of new firms, etc. The system's performance thus depends heavily on the established roles of established companies, helped by local and national banks.[4] (The name "corporatism" fell into disuse after the second world war and was replaced by the *social market* in Germany, *concertazione* in Italy and *social democracy* in France. Yet some French politicians and journalists freely speak of *corporatisme*. In any case, the western continental European economies are still importantly corporatist, including those in the big 3 – Germany, France and Italy – both in structure and in intent.[5])

Today economists view capitalism as having evolved into a rousing system for cutting-edge innovation and view corporatism as designed for industrial peace, social consensus and community stability – Mars and Venus, roughly speaking.

The thinking in the second half of the '20s was more nearly the opposite. In 1927 Italy was suffering the effects of an exchange rate stabilization similar to Britain's crisis over its revaluation of the pound and it was at that time that Mussolini abandoned the experiment with neoclassical policies and sought the ideas for revamping the economy that would be dubbed corporatist. The redesign was to *go for growth*. Severini's *futurist* paintings came to symbolize the aim of the new economic policy. The economic historian Marcello de Cecco comments on the added purpose, writing about this period, remarks:

> The limits and modes of State intervention were to be established not by theory but by necessity, and the only imperative was that of making the country as rich and powerful as was possible, given the constraints that existed at all times.[6]

Yet the Italians did theorize. Many of the corporatist theoreticians thought that the corporatist system beginning to take shape in 1927 would be *more* dynamic than capitalism – maybe not more fertile in little ideas, such as might come to petit bourgeois entrepreneurs, but certainly in big ideas. Not having to fear fluid market conditions, an entrenched company could afford to develop expensive innovations based on current or developable technologies. And with industrial confederations and state mediation available, such companies could arrange to avoid costly duplication of their investments. The state for its part would promote technological advances in cooperation with

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[3] With the rise of the market economy these bodies were criticized as monopolistic and in the French Revolution the D'Allarde Decree abolished them, though many managed to come back.

[4] A recent survey of the strains of corporative economic thought in interwar Italy is Marco E. L. Guidi, "Corporative Economics qnd the Italian Tradition of Economic Thought," in *Storia del Pensiero Economico,* No. 40, 2000/I. The paper is available at www.dse.unifi.it/spe/indici/numero40/guidi.htm I have placed an excerpt in the Appendix.

[5] Since the second world war, some of them may have became less corporatist with the liberalizations that reduced the monopoly power of firms and banks (as in France). In most of them, however, new corporatist institutions have sprung up: Codetermination (*cogestion*, or *Mitbestimmung*) has brought "worker councils" and in Germany a union representative generally sits on the investment committee of the corporation.

[6] Marcello de Cecco, "Keynes and Italian Economists," ms., Fiesole, ca. 1983, p. 19. The author emphasizes that some of Mussolini's new economic policy of 1927 had roots in anti-liberal ideology of pre-Fascist times.

industry.[7] The state could indicate new economic directions and favor some investments over others through its instrument, the big banks. In the eyes of these theoreticians, then, the system's purpose was a mobilization of the nation's collective knowledge – a view that might be termed *scientism*.

The Corporatism in Keynes

Keynes in the mid-'20s confronted an economic system in Britain that suffered many of the stresses that Mussolini's new economic policy aimed to solve. And Keynes, then in his early 40s, was not too old to be intrigued by the new arguments against the Smithian economic model coming out of Italy. In fact, Keynes's political economy showed some parallels with corporatist thinking. Some of these parallels are in the area of industrial organization theory and industrial policy

Keynes an exponent of top-down growth Contrary to American impressions that his microeconomics was neoclassical – more than Marshall's was – Keynes rejected atomistic competition as an efficient market form. The policy he advocated called for the government to assist the ongoing movement toward cartels, holding companies, trade associations, pools and others forms of monopoly power; then the government was to regulate the affected industries.[8] "In the 1920s at least," James Crotty concludes, "Keynes was unabashedly corporatist, supporting a powerful microeconomic as well as macroeconomic role for the state."[9]

Such a wave of consolidation and unionization did occur to varying degrees in the 1930s not only in the U.K. but also on the European continent and in the United States. In the U.S. by the end of the decade, there were three giant auto makers where there had been tens of companies in the early 1920s. The Temporary National Economic Committee (TNEC) was established by Congress in 1938 to advise on the regulatory and dissolution questions posed by the oligopolistic organization of much of American industry. This was the corporatist-tinged system that prevailed in the U.S. from the presidential terms of Franklin Roosevelt through those of Richard Nixon, whereupon it began to erode and, in places, to break up with anti-trust break-ups, deregulation initiatives and global competition.

Was this modified system for the good, as Keynes and the corporatists believed? The economies of scale, Chandler's economies of scope, and the dynamic economies of "learning," or practice, on the repetitive assembly line that were achieved over the span of consolidation/rationalization (leaving aside the unionization, which may not have helped) running from 1920 to 1941 must have been extraordinary. The increase in hourly productivity and of total factor productivity over both those decades were unprecedented and have not been matched since (with the possible exception of the past 10 year span). Hitler marveled at the stunning productivity level at the Ford Motor plant, according to

[7] A presidential decree of February 1919 established a board "aiming at preparing a projected constitution for a National Research Council," the purpose of which was "the planning and promotion of researches for science and industry" along with national defense. The CNR came into being with a decree in November 1923. A similar body in France was formed in 1939. The U.S. National Science Foundation was created only in 1950 "to promote the progress of science; to advance the national health, prosperity, and welfare; to secure the national defense…"

[8] Two of these statements are Keynes, "The End of Laissez Faire," reprinted in *Essays in Persuasion*, and the Liberal Party publication, *Britain's Industrial Future* , (1928).

[9] James Crotty, "Was Keynes a Corporatist? Keynes's Radical Views on Industrial Policy and Macro Policy in the 1920s," *Journal of Economic Ideas*, 33 (3), September 1999, 555-578. A reviewer in Amazon.com argues that Keynes's agenda was no different from that of the 1912 Progressive Party of Theodore Roosevelt.

records of his "table talk" in the early 1940s. But was this system better at *innovating* than was the system of the 1920s that it replaced? In the judgment of Joseph Schumpeter in 1944 the answer was yes. That is also the verdict of our own William Baumol in his 2003 book.[10] But the econometric results are not in – not yet, although it is safe to say that they are now not far off. In an excoriating attack on that period, Carl Schramm sees it as having been replaced in successive steps beginning in the 1970s by a more nearly capitalist system that is far more innovative than the semi-corporatist system was.[11]

In the late 1930s and early 1940s Friedrich Hayek was to initiate a modern theory explaining how a capitalist system, if not too weighed down with imperfections and departures, would possess the greatest dynamism – not socialism and not corporatism.[12] 1st, virtually everyone right down to the humblest employees has arcane "know-how," some of it what Michael Polanyí called "personal knowledge" and some merely private knowledge, and out of that an idea may come that few others, if any, would have.[13] In its openness to ideas of all or most participants, the economy tends to generate a plethora of new ideas. 2nd, the pluralism of experience and knowledge that the financiers bring to bear in their decisions gives a wide range of entrepreneurial ideas a chance of an informed, insightful evaluation. And, importantly, the financier and the entrepreneur do not need the approval of the state or of social partners. Nor are they accountable later on to such a social body if the project goes badly, not even to the financier's investors. So projects can be undertaken that would be too opaque and uncertain for the state or social partners to endorse. 3rd, the pluralism of knowledge and experience that managers and consumers bring to bear in deciding which innovations to try and which of those to adopt is crucial in giving a good chance to the most promising innovations launched. Where the Continental system, acting in the spirit of scientism, convenes experts to set a product standard before any version is launched, capitalism gives market access to all versions – an inconvenience that pays off later.

Keynes writing in the mid-'20s knew nothing of such an argument. Keynes must have reflected upon the theorizing of the Italian corporatists and of Theodore Roosevelt's Progressive Party but could not have encountered the Hayekian argument for the superior innovativeness of capitalism. There is nothing in his writings up to that time that suggests he would have been attuned to it.

Keynes disdainful of the quest for wealth Keynes was blind to almost all of the satisfactions that might come from an economy of real dynamism. He brilliantly grasped the results of Frank Ramsey on the optimality of growing through capital formation until some sort of "bliss" level of satisfaction is reached: After all, he had inspired Ramsey to do the analysis and he provided Ramsey with an intuitive explanation of the algebraic formula for the optimum rate of saving. Keynes's "Economic Possibilities for our Granchildren" reflects in several passages his clear understanding of the benefit – mainly in the form of rising leisure – that comes from capital accumulation: from piling on more and more machinery until the marginal productivity of it has ceased to justify any more capital deepening. He appeared to see no satisfactions from the growth process.

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[10] J. A. Schumpeter, *Capitalism, Socialism and Democracy*, New York, Harper & Bros., 1944; W. J. Baumol, *The Free-Market Growth Machine*, Princeton, Princeton University Press, 2003.

[11] C. J. Schramm, "Entrepreneurial Capitaism and the End of Bureaucracy," Annual Meetings, American Economic Association, Boston, January 2006.

[12] F. A. Hayek, *The Economic Order*, London, 1937, and *The Road to Serfdom*, London, 1943.

[13] A column in the Wall Street Journal told of a deliveryman who was asked whether he found it best to work from the top floor down or the reverse. "It depends on the time of day," he replied. A beautiful Hayekian moment.

This attitude of Keynes – unusual for an economist – was emblematic of the intellectual current in Europe at that time called *anti-materialism*. That strain in social thought was the main theme of the "Christian corporatism" that arose on the Continent in the second half of the 19th century: an indifference to business life and a devaluation of wealth, its accumulation and its holding. The 1893 Papal Encyclical of Leo XIII, *Rerum Novarum*, is all about the higher value to be placed on life, community and worship compared with the materialist satisfactions of, say, consuming and earning. From this point of view, the commercial economy is no more than a regrettable necessity. That view of the world was yet another strain in 20th century economic corporatism, which sees a conflict between employee and shareowner, between one employee and another and between one company and another but did not see know-how, entrepreneurship and innovation as driven by various materialist desires including the pursuit of wealth, know-how and fame.

Keynes and the corporatists did not understand that much of the huge rise of productivity that the world was to see from 1920 onward would be traceable to new commercial products and new business methods that could only have been developed and launched in the relatively capitalist economies;[14] and that if increased wealth, which successful innovations result in, is denigrated, that would constitute one more "minus" among the pluses and minuses of undertaking innovative projects and that such an effect would put a premature end to economic growth.

Keynes blind to the intellectual satisfactions in business life Corporatism did not comprehend that an economy fired by the new ideas of entrepreneurs serves to transform the workplace – in the firms developing an innovation and also in the firms dealing with the innovations. The challenges that arise in developing a new idea and in gaining its acceptance in the marketplace and the challenges to management and consumers in figuring out how and whether to adopt the latest innovation provide the workforce with high levels of mental stimulation, problem solving and thus employee engagement and personal growth. (Note that an individual working alone cannot easily create the continual arrival of new challenges. It takes a village, better yet the whole society.)

Is there any precedent for thinking that people – virtually all people – value such stimulation, mastery, growth, discovery? The concept that they do originates in Europe: There is the classical Aristotle, who writes of the "development of talents," later the Renaissance figure Cellini, who jubilates in achievement and advancement, and the baroque writer Cervantes, who evokes vitality and challenge. By the early part of the 20th century economists Alfred Marshall and Gunnar Myrdal write that engagement in the job is already hugely important in the advanced economies. It may be that this view, sometimes called *vitalism*, is now strongly associated with the pragmatist school founded by the American William James to which Henri Bergson in France and John Dewey in the U.S. belonged. The American psychologist Abraham Maslow coined "self-actualization" and John Rawls the terms "self-realization" to refer to a person's emerging mastery and unfolding scope. (Amartya Sen has referred to "expanding capabilities to do things.") These two Americans understood that most, if not all, of the attainable self-realization in modern societies can come only from career. We cannot go

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[14] These include household appliances from vacuum cleaners to refrigerators, sound movies, frozen food, pasteurized orange juice, television, transistors, semi-conductor chips, the internet browser, the redesign of cinemas, and the recent retailing methods. (Of course there were often engineering tasks and technical advances required along the way, yet business entrepreneurs were the drivers.)

tilting at windmills, but we can take on the challenges of career. If a challenging career is not the main hope for self-realization, what else could be? Even to be a good mother it helps to have the experience of work outside the home.

The *solidarism* that is a part of corporatist culture militates against a life of such personal development. Although anti-materialism led to a certain devaluation of wealth, and thus also to frowning on any visible efforts at increasing the amount of observable wealth one possessed, the idea of solidarism sees it as unacceptable to move out of one's place in the community. In a solaridist society people who go to great lengths to stand out in their group or to escape their group are hated.

Alas, Keynes conveyed no sense of the role of innovation in imparting excitement and personal development to business careers. Nowhere is this clearer than in his famous passage in "Economic Possibilities of our Grandchildren":

> …[I]f we look into the past, we find that the economic problem, the struggle for subsistence, always has been hitherto the primary, most pressing problem of the human race…If the economic is solved, mankind will be deprived of its traditional purpose. Thus for the first time since his creation man will be faced with his real, his permanent problem – how to use his freedom from pressing economic cares, how to occupy the leisure, which and compound interest will have won for him, to live wisely and agreeably and well.
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> For many ages to come the old Adam will be so strong in us that everybody will need to do *some* work if he is to be contented….When the accumulation of wealth is no longer of high social importance, …we shall be able to rid ourselves of many of the pseudo-moral principles which have hag-ridden us for two hundred years, by which we have exalted some of the most distasteful of human qualities into the position of the highest virtues.[15]

The most basic of these is that nowhere does Keynes recognize the wisdom of the pragmatist school – from James to Dewey to Rawls and on to Sen – that people need to exercise their minds with novel challenges – new problems to solve, new talents to develop. A mistake like that in the initial premise dooms the essay to misguided conclusions, such as the conclusion that people will learn simply to enjoy things without any effort.

But if Keynes *had* recognized that people *need* a system that throws out problems to challenge the mind and engage the spirit, he would still have gone wrong because he never saw that with the technical progress and capital deepening that he aptly postulates, an ever-increasing share of people can *afford* jobs that are stimulating and engaging; so unless the economic system is prevented from doing so, more and more jobs will be *supplied* that offer stimulation and engagement. So, were working-age people not to work or to work only a few hours a week, a great number of them would find themselves deprived of the fruit that is the special prize of the most advanced economies. The only persuasive position to take is that, with steady technical progress, an increasing number of jobs will offer the change and challenge that only the predominantly capitalist economies, thanks to their dynamism, can generate.

These thoughts point to what might be called the Keynes Puzzle and the likely

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[15] Keynes, "Economic Possibilities for our Grandchildren," *Atheneum*, 1930, reprinted in *Essays in Persuasion*, London, Macmillan, 1932; New York, Harcourt Brace, 1932.

answer to it. The *puzzle* is that, if we accept Keynes's psychological and economic framework, which is essentially that of Frank Ramsey, we should expect to see the workweek shrinking over the centuries to next-to-nothing, as Keynes made explicit; and yet we see nothing of the kind. It is a fact – notorious among some social critics – that in the United States the workweek has shrunk little if at all in recent decades. Indeed, as more and more people work in the financial industry and the legal profession, we may see the mean work week begin to reverse field and rise toward some steady-state level higher than it is now. The *answer* to the puzzle is that work is *not everywhere an inferior good*. It is locally inferior at an onerous work level but not at levels so low that they would deprive of us of some of the stimulation, challenge and personal development we can find in our careers. The fact that work has not come to an end in some Ramseyan march toward "bliss" is *strong evidence* of the fallaciousness of the Keynes-Ramsey theory of what people want and where, accordingly, societies are headed – if they haven't already got there.

The Legacy of Corporatism

Keynes's thinking nevertheless proved prophetic in a way. Most of the Continental economies, including even the largest ones, though repeatedly able to catch up *technologically* with the world's "lead economies" after one or more of the latter have spurted ahead, continue to exhibit sub-par innovation, job satisfaction and employee engagement. As a result, a range of social and economic indicators, from birth rates and emigration to participation rate and unemployment, continue to signal the stultifying influence of corporatist culture and policy on the Continent.