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**MARX AND SCHUMPETER:
A COMPARISON OF THEIR THEORIES OF DEVELOPMENT**

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Marx and Schumpeter: A Comparison of their Theories of Development

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Abstract

This paper aims to draw out the similarities and differences between the theories of Marx and Schumpeter. This is done first, by discussing the methods the two use and second, by examining the different aspects of their theories. It is argued that Marx's 'materialist conception' has two logically separate parts. In one of these social reality is seen in organic terms, in a constant process of change driven primarily by economic forces. The other refers to the phenomenon of social classes. In general, Marx adopts the view that every society is split between two social classes, those who own means of production and those who live by their labour. It is in these terms that Marx conceptualises capitalism. Schumpeter adopts, with some interesting modifications, the first part of Marx's 'conception' which he calls the Economic Interpretation of History. And he rejects the second, and develops his own theory of classes, in which the phenomenon of social classes rests essentially on differences in aptitudes of individuals in a society. The paper attempts to show that the similarities and differences in the development theories of the two authors are derived essentially from the similarities and differences in their methods. Schumpeter's enormous respect and admiration for Marx is based on the latter's 'discovery' of the method of Economic Interpretation of History and second, on Marx's attempt to construct an all-embracing framework for analysing economic and social change.

In his Introduction to the Japanese edition of his Theory of Development, Schumpeter wrote:

It was not clear to me at the outset what to the reader will perhaps be obvious at once, namely, that the idea and the aim are exactly the same as the idea and aim which underlie the economic teachings of Karl Marx. In fact, what distinguishes him from the economists of his own time and those who preceded him was precisely a vision of economic evolution as a distinct process generated by the economic system itself. In every other respect he only used and adapted the concepts and propositions of Ricardian economics, but the concept of economic evolution which he put into an unessential Hegelian setting, is quite his own. It is probably due to this fact that one generation of economists after another turns back to him again and again although they may find plenty to criticise him. I am not saying this in order to associate anything that I say in this book with his great name. Intention and results are much too different to give a right to do so. Such similarities in result as undoubtedly exist ... are not only obliterated by a very wide difference in general outlook but also reached by such different methods that showing parallel lines would be highly unsatisfactory to Marxians. But I wish to point to their presence because readers trained in Marxian economics may find the reading of the book facilitated by this reference and also may be interested in comparisons. Schumpeter's *Essays* edited by R.V. Clemence, Reading, Mass., Addison Wesley, 1951:160-61.

Samuelson categorically rejected the view regarding the similarities between Schumpeter's and Marx's works. He wrote:

I am of course aware that Schumpeter has in many places articulated words of praise and admiration for Karl Marx. But I and other of his students found this puzzling since in neither his lectures nor his writings could we identify the reasons for this admiration. It would be an evasion for us to write it all off as typical Schumpeterian empty praise –as when he would introduce to Harvard audiences with flowery compliments the Mises he looked down on and the Hayek whom he considered overvalued. Somehow his respect for Marx was more long lasting and seemed genuinely sincere. Despite repeated investigations I never could find the answer to the puzzle. Indeed in the end the evidential record requires me to conclude that, even if under hypnosis Schumpeter were to insist on the genuineness of his admiration for Marx, careful comparison of how the two writers would interpret dozens of different questions and processes will reveal that Schumpeter's answers are 180 degrees from Marx's – and the differences are generally precisely those differences that neoclassical

pendants have with Marxian writers. Pragmatically what counts is not a scholar's rhetoric but rather his substantive hypotheses and descriptions.'

P.A. Samuelson, 'Homage to Chakravarty: Thoughts on his Lumping Schumpeter with Marx to Define a Paradigm Alternative to Mainstream Growth Theories' in *Capital, Investment and Development: Essays in Memory of Sukhamoy Chakravarty*, edited by Kaushik Basu, Mukul Majumdar and Tapan Mitra, Oxford, Blackwell, 1993: 250-51.

1.

It will be noted that in the first quotation above, Schumpeter speaks of the similarities between his own and Marx's works only in respect of a vision of economic evolution or, what is the same thing, theory of development. We know that Schumpeter has no sympathy whatever with Marx's 'adaptation' of Ricardian 'concepts and propositions' – a reference to Marx's labour theory of value. Schumpeter regarded Ricardian economics in general and theory of value in particular as a 'detour', a departure from the main line of the historical development of economic analysis. Marx's value theory he regarded in the same light – as an aberration.¹ Although it would be interesting to explore Schumpeter's reasons for declaring the Ricardian-Marxian theory of value as a 'detour', to keep the discussion manageable the focus of the present discussion is entirely on the theory of development. Is there, in this area, a common ground between Schumpeter and Marx, as Schumpeter suggests? What are the ideas that make up this common ground? And, what are the differences, if any? By discussing the theories of the two authors, this essay reflects on these questions.

2.

To set the stage for the discussion that follows, we start with the nature of the problem under consideration. From around the middle of the eighteenth century, the modern capitalist or market economy in Western Europe was becoming visible in its broad outline. Although 'mercantilist' restrictions on economic activity were by no means things of the past, there had been sufficient development of the economy (particularly in England) for economic and social thinkers of the time to attempt to conceptualise or to 'model' it in terms of market relations. There were obvious differences between the new emerging economy and that which had preceded it. The latter was characterised by restrictions and monopolistic privileges conferred by the sovereign, and before that by feudal relations on land and corporatist restrictions in cities. By contrast, in the economy taking shape in the eighteenth century, labour was becoming increasingly mobile between occupations and capital was

¹ *History of Economic Analysis*: 474. For details of works cited, see 'References' at the end of this paper.

increasingly able to move between industries without restrictions. This had the makings of a full-fledged market economy and it was only now that it could be conceptualised in terms of market relations.

A market economy, by definition, is unmanaged and unregulated. In it individuals make their economic decisions independently of each other. This raises the question as to how these decisions come to be coordinated and harmonised? In other words, what is the internal logic of this economy that enables it to maintain its balance or equilibrium? This problem – raised famously by Adam Smith's analogy with 'an invisible hand' - became the subject matter of what later came to be known as 'equilibrium theory'.

At the same time social thinkers of the period also began to raise questions regarding the phenomenon of economic progress, a phenomenon with which the eighteenth century had become deeply imbued. Adam Smith (the title of whose magnum opus directed attention to this phenomenon) and his fellow philosophers of the 'Scottish Enlightenment', for instance, saw human society developing through certain definite stages.² Looking across the world, they observed different forms of economic and social organisation. They saw these 'modes of production' or social orders as different stages in the progress of human society. It was as if these societies were at different rungs of the same ladder reaching towards the great prosperity and wealth that the commercial society then taking shape in Europe promised.

These discussions raised questions such as: What are the levers of progress? What is the internal logic through the working of which human society moves from one stage of development to the next? Is there here also perhaps 'an invisible hand' that translates individual desires and self-motivated actions towards the goal of increasing economic wealth and social progress? It was to be the task of the theory of development to address these questions. The main works both of Marx and Schumpeter fall in this line of inquiry.³

3.

The present section and the one that follows outline those elements of Marx's thought with which Schumpeter is in broad agreement and which, with some important and interesting modifications (to be discussed later), he uses to underpin his own theory of social evolution. These elements of Marx's thought I will refer to as Marx's materialist method or materialist

² Adam Smith identified four stages in the development of human society. There were: hunting, pastoral, agricultural (feudal) and commercial (the capitalism of his day). See *The Wealth of Nations*, Book II, Chapter I.

³ This statement needs to be qualified. Following in the footsteps of David Ricardo, Marx spent an enormous amount of effort developing his own equilibrium system which shows how values, surplus values and profits are

hypothesis. Schumpeter prefers to call this set of ideas as Economic Interpretation of History because he thinks this term to be philosophically neutral. In section 5, I will discuss those aspects of Marx's approach to historical development which though crucial for Marx's schema and Marxism generally have no place in the Schumpeterian system.⁴ Section 6 will outline Schumpeter's modifications of Marx's method and the hypotheses that he puts in place of those aspects of Marx's approach that he rejects.

First, Marx sees society as an organism whose different parts complement each other and perform life-preserving functions. No individual part of this structural whole, be it religion, family life, the educational system, scientific activity, etc., can be understood in isolation from other aspects of social life. In the economic sphere, the organic nature of society shows itself in the social division of labour and interdependence between different activities. We note that in a system thus visualised change in one part of the organism to be accomplished would require appropriate adaptations in other parts of the system. The process of development thus becomes a process of adaptation of various parts of the organism to any 'initial' change in one or more parts.⁵

Second, Marx sees social phenomena as a historical process in constant change. Engels was referring to this aspect of Marx's vision when, acknowledging his and Marx's debt to Hegel, he wrote that the great merit of the latter's philosophy was that the natural, historical and spiritual aspects of the world were 'represented as a process of constant transformation and an effort was made to show the organic nature of the process'.⁶ Marx conceptualised this process as one in which society reproduces itself in time. Thus, each generation inherits its physical capital, its stock of knowledge, value systems and culture from the preceding generation, acts on this inheritance, enriches it and passes it on to one that follows. This is historical development or social evolution. Marx was expressing this idea when he wrote: 'Men make their own history, but they do not make it just as they please; they do not make it

determined. But it is the case that this system is developed to serve the needs of his theory of economic and social evolution of capitalism.

⁴ The full range of Marx's ideas on his materialist approach was christened by Friedrich Engels, Marx's close friend and collaborator, as the 'materialist conception of history, also as 'historical materialism'. Marx seems not to have used either of these terms. In the 'Preface' to *A Contribution to a Critique of Political Economy*, he referred to his general materialist approach as 'the general result' which 'served as a guiding thread throughout my studies' and in the 'Preface' to the second edition of *Capital*, vol. 1 he referred to it as 'the materialist basis of my method.' Marx's formulations of the method can be found in the *German Ideology* (written with Engels), 'Letter to P. V. Annenkov', the *Communist Manifesto* (written with Engels), and 'Preface' to *A Contribution to a Critique of Political Economy*. For a good illustration of Marx's actual use of his method to discuss historical events, see his *Eighteenth Brumaire of Louis Bonaparte*.

⁵ According to Schumpeter all social phenomena needs to be understood as 'adaptations to existing needs'. See his *Imperialism and Social Classes*: 109.

⁶ F. Engels, *Socialism, Utopian and Scientific*:132. Schumpeter also emphasises the historical nature of the social process. For instance, he writes that the 'social process is a unique process through time, and change is

under circumstances chosen by themselves, but under circumstances directly encountered, given and transmitted from the past.’⁷

Third, there is the assumption that social reality evolves through some ‘internal necessity’; that there is some thing inherent in the social organism that causes it to undergo constant change on its own accord. In other words, no external force is needed to move it, as ‘the analogy of Newtonian mechanics suggests’.⁸ We should note that without this assumption (that change is truly endogenous, that there is something inherent in the system that makes it move on its own accord) historical development will simply be the result of unpredictable exogenous influences and there would be no theory of development. With this assumption it becomes the task of the theory of development to identify the inherent or endogenous force that provides the ‘prime mover’ of change, and suggest the manner in which economy and society internally adapt to initial changes. A corollary of this way of looking at the social process is that any theory or model devised to study economic phenomenon in its stationary state, or that conceptualises the economy in static terms, will not be adequate for the task of studying ‘constant and irreversible’ change that arises from the very nature of the organism. An analytic apparatus formulated specifically for the purpose of studying the economy as a process of change will be needed.

4.

The basic idea underlying Marx’s materialist method was expressed by him in one of his *Theses on Feuerbach*. According to this ‘thesis’: ‘Social life is essentially *practical*. All mysteries which mislead theory into mysticism find their rational solution in human practice and in the comprehension of this practice.’ The same thought was reiterated many years later when Marx recalled the period when this idea was first formulated. He wrote: ‘My investigations led to the result that legal relations as well as forms of state are to be grasped neither from themselves nor from the so-called general development of the human mind, but rather have their roots in the material conditions of life, the sum total of which Hegel ...

incessant and irreversible’ and ‘incessant and irreversible change [is] the most obvious characteristic of social phenomena’. *History of Economic Analysis*: 435-37.

⁷ *The Eighteenth Brumaire of Louis Bonaparte*: 247. The concept of reproduction is an essential part Schumpeter’s thinking about the problem of social evolution, as we will see below. For instance, he writes: ‘Every social situation is the heritage of the preceding situations and takes over from them not only their cultures, their dispositions, and their ‘spirit’, but also elements of their social structure and concentrations of power.’ *Imperialism and Social Classes*: 111.

⁸ While discussing Hegel’s ‘evolutionism’, Schumpeter writes: ‘... the reader will observe that of Hegel’s emanist conception of evolution something remains, even if we drop its metaphysical trappings, namely, the idea or perhaps discovery that reality, as we know it from experience, may be in itself an evolutionary *process*, evolving from inherent necessity, instead of being a set of phenomena that seek definite state or level, so that an extraneous fact – or at least a distinct factor – is necessary in order to move them to another state or level as the analogy with Newtonian mechanics suggests.’ *History of Economic Analysis*: 437.

combines under the name of 'civil society', that, however, the anatomy of the 'civil society' is to be sought in political economy'.⁹

We have here the idea that society's social structure and its general institutional framework and cultural and value-systems are functions of existing material conditions, at the core of which lies the structure of production or the technological-economic base. As he put it rather graphically in one of his earlier expositions of this method, the social structure and beliefs and value-systems of the feudal economic and social organisation rest on the foundation of the hand-mill type of technology, while the social structure and culture of the capitalist society (of his day) rest on methods of production as embodied, for instance, in the steam-mill. The feudal social organisation and value-systems would be entirely incompatible with the kind of technology that provided the basis of the nineteenth century capitalist society, just as the later would be inconceivable as resting on the hand-mill type of methods of production. Thus, the hypothesis emphasises, in the first instance, the complementarity or organic relation between methods of production, economic, legal and social institutions, and the value-systems of society, and second, it assigns relative autonomy to the economic and technological infrastructure of society.¹⁰

For Marx, this idea provides the key to understanding historical development or social evolution. That is, changes in the nature of social organisation, social and cultural institutions, the way we live, do philosophy, interpret religion, etc., are all function of changes in economic conditions or economic evolution. The economy develops according to certain 'internal necessities', and changes in social, political and cultural conditions are the 'necessary' adaptations to changes in forms of production and the economy in general. These adaptations or adjustments arise spontaneously (through the actions of individuals), incrementally and in response to needs created by changes in the organisation of production. The cumulative effect of these changes in the long run is to alter the structure and nature of social organisation and with it our belief systems. We note that there are two

⁹ 'Preface' to *A Contribution to a Critique of Political Economy*.

For Schumpeter's 'materialist' approach – the importance of the economic factor as the basis of our rational thought and logic, see his *Capitalism, Socialism and Democracy*, the chapter entitled 'The Civilisation of Capitalism'. For instance, he writes (pp. 122-23): 'Now the rational attitude presumably forced itself on the human mind from economic necessity; it is everyday economic task to which we owe our elementary training in rational thought and behaviour – I have no hesitation in saying that all logic is derived from the pattern of economic decision ... Once hammered in [in the sphere of production] the rational habit spreads under the pedagogic influence of favourable experience to other spheres of life and there also opens eyes to that amazing thing – the Fact.'

¹⁰ Schumpeter points out that in emphasising the autonomy of conditions of production or the material base on which the 'superstructure' of value-systems, etc., is based, Marx was not saying that 'religion, metaphysics, schools of art, ethical ideas and political volitions were either reducible to economic motives or of no importance. He only tried to unveil the economic conditions which shape them and which account for their rise and fall.' *Capitalism, Socialism and Democracy*: 10.

sub-hypotheses here: one relates to economic evolution (taking place autonomously through some internal necessities), the other to social evolution which is the necessary concomitant of economic evolution.

This is the central idea of Marx's materialist hypothesis. But we should add a further consideration to it. The idea that social and cultural change is a function of autonomous changes in conditions of production needs to be understood in historic-organic, not mechanistic, terms. We do not see technology as an independent variable, on one side of the equation, and social and political change as the dependent variable on the other, the former 'determining' the latter. New methods of production grow organically out of society's attempts to deal with the problems that economic development creates, and their successful adoption depends not only on the existing technical and economic conditions, but also on the prevailing social and cultural environment. Thus, it is not the case that any new technology can be successfully incorporated into the production system, nor that a technique developed and found appropriate in one economic and social environment can normally be implanted in another with equal efficiency. Although we treat technical changes as autonomous factors in the process of development we need to remember that they are themselves generated within the same process of economic and social change. Just as (according to Marx) there is no such thing as the history of ideas or the 'so-called general development of the human mind', there is also no such thing as the history of technology or history of the economy. There is only history of society.¹¹

To conclude this section: Marx's materialist method is an approach to studying economic and social development in which society is conceptualised as an organism in a process of constant change, that is self-evolving through the working of some endogenous force or necessity that is essentially economic in character. Schumpeter adopted this general viewpoint, which he considered as ideologically neutral, as a working hypothesis for his own theory of economic and social development.

5.

We turn now to the other aspect of Marx's general materialist approach which Schumpeter considers to be logically separable from the method outlined in the preceding paragraphs and which according to him is ideologically inspired. We may have some doubts about the philosophical neutrality of the Economic Interpretation of History, but there is no doubt that it is through this 'additional' hypothesis that Marx's political philosophy enters his general

system of thought. Since it is at this point that Marx and Schumpeter go their separate ways, it is useful to note the nature of the hypothesis we are now considering. The materialist method or hypothesis outlined above tells us about the way that we conceptualise society in general— we see it in organic terms, and undergoing constant change driven by economic forces. But it postulates nothing about the specific nature of the society we are considering and the nature of the economic necessities that cause it to change. For instance, it says nothing about whether the society is tribal or capitalistic; and if it is capitalistic, it says nothing about whether this system is class ridden and exploitative or class-less and welfare generating; it makes no assumption about the nature of the ‘inner necessities’ that cause it to change and develop. The Economic Interpretation of History (as outlined above) is like a black box; the ‘additional’ hypothesis to be discussed in the present section is the content that Marx puts into this box.

The ‘additional’ hypothesis of Marx refers to his theory of social classes and the related concept of the mode of production. This hypothesis is the centrepiece of Marx’s entire thought; it gives unity to all his thinking on economic and social questions. Marxism will not be Marxism without it. It is through this hypothesis that Marx identifies the nature of the capitalist mode of production. It provides the basis of his thinking on the theory of value, profit and accumulation, and it implements his conception of social evolution. According to this hypothesis social evolution takes the form of a succession of modes of production, transition between them being effected through class struggle. History of society becomes the history of class struggle.

Marx locates the existence of social classes in the sphere of production, in particular in the ownership of the means of production. And the relationship between classes, one owning the means of production and the other living by its labour alone, becomes the focal point of social structure. Directing his attention to any given situation of production methods and level of social product, Marx argues that the relationship between the two classes must necessarily be one of antagonism. This is the case because given the level of social product more for one means less for the other. It is true that there are other tensions in society, for instance, between producer and producer who must compete for markets, between worker and worker who compete for jobs, between one religious or ethnic group and another. However, Marx assumes that the commonality of economic interests among property owners on the one hand and among those who live by work alone on the other will dominate over intra-class tensions. Thus, class conflict between those who possess means of production

¹¹ On this, see Marx's discussion in the 'Introduction' (section 'The general relation of production to distribution

and, by virtue of that, economic and political power and those who labour for them becomes for Marx the central 'contradiction' in society – a 'contradiction' that can only be resolved by a fundamental change in the property relations of society or, what is the same thing, change in class structure or change in the mode of production.

This standpoint is underpinned by a further interpretation of the materialist method according to which (as we saw earlier) society's ideological 'superstructure' is a function of material conditions of life. Conditions of production determine social structure and through it (to use Schumpeter's words) 'all manifestations of civilisation and the whole march of cultural and political history'. But social structure is seen entirely in class terms. Thus 'all manifestations of civilisation' come to be determined by existing class relations or, what comes to the same thing, property relations. The idea is quite simple: a person's economic life-situation determines his outlook on life and his way of understanding and interpreting economic and political issues of the day. It follows that members of a social class, having similar economic needs and sharing essentially the same economic life-situation, will come to share the same outlook on social questions.

Thus, given that there are two social classes, ranged on opposite sides of the production system and each with distinct economic interests, we should find, broadly speaking, two competing world-views in society. One sanctions the prevailing property relations and power structure and declares the existing social order as just and immutable. This is the ideology of the ruling class. This ideology prevails because the dominant class has all the means to disseminate it. However, with the development of the economy the oppressed class gains in strength and class-consciousness and eventually learns to articulate its own ideology and use it as a weapon in its struggle against the ruling class.

We take up now the other, but related, aspect of Marx's thinking on historical development: that it takes the form of succession of modes of production. A mode of production is a *distinct* type of economic and social organisation, its central feature being the form in which property is held and the form that relations between owners of property and direct producers takes. Each mode of production thus has its own unique value and belief systems. In his early writings (*The Communist Manifesto*, for instance), Marx identified three modes of production that history had by then witnessed. These were: the 'ancient', based on slave labour, the feudal, characterised by labour's bondage to land, and capitalism, with its juridically free labour and competitive labour market.

and exchange') to his *Grundrisse: Introduction to the Critique of Political Economy*.

When a mode of production comes into existence it is progressive in character, that is, relatively to the one it succeeds.¹² Most of the barriers that the preceding mode had placed on economic progress are swept away, and new institutions develop to suit the requirements of economic development, which coincide with the needs of the new ruling class. During this period of development, the ruling class performs necessary social functions. There is progress toward greater rationality and humanity, the exploitative character of the ruling class notwithstanding.

However, there comes a time when the process of institutional adaptation to changing economic and social needs begins to falter. Strains and tensions develop in the system; there is a state of imbalance between the requirements of economic development on the one hand and the economic and legal institutions (property relations) on the other. As a result an economic and social crisis ensues.

Two questions arise: how do we explain the maladjustment between the forces of production or economic development and 'property relations'? And, how is the crisis resolved? We know that economic development requires appropriate adaptations in the institutional frame of society. In the early stages of development within the existing mode of production (as we have seen) appropriate institutional adjustments were taking place to keep in step with progress in the forces of production. It was so because these changes were in the interests of the propertied-ruling class that had come to power with the emergence of the new mode of production. But now economic development has reached a point where it requires changes that the dominant class is unable and unwilling to make. That is the case because these changes threaten the existing power structure of society. The class that had formerly led the way in institutional change has now become conservative. Thus, it can take the society no further. It is an essential part of Marx's general approach that at some point in its life the mode of production undergoes a process of ossification. It fails to deliver progress.

But, according to the hypothesis, this failure does not stop progress. The process of development, as it creates problems, also generates the forces that find solutions to those problems. That is after all what it means to say that the process of development is endogenous in its nature. In fact, the old mode, in the course of its development, has already

¹² Although Marx expressed this hypothesis in general terms as a grand narrative of universal human history, his scientific work was entirely devoted to understanding *capitalist* development, to discovering the 'laws of motion' of capitalism. When reading these passages outlining this general hypothesis, the reader may find it helpful to interpret them as primarily applying to capitalist development, a mode of production that succeeded feudalism and will be succeeded by socialism. See section 7 below.

created the forces that will take society forward. These forces are represented by the oppressed class. In the course of development this class learns that within the existing institutional frame there is little scope for any improvement in its living conditions; it grows in class-consciousness and learns to articulate its own ideology. Given the economic and social crisis that has gripped society, it can speak for the entire society. It is ready to seize political power. We note that, at the same time, the development within the old mode of production has also created all the material conditions for the new mode. The latter has also been gradually evolving within the 'womb' of the old mode. The development process in the old mode of production has thus created both the cultural and the physical infrastructure for the new order. The scene is thus set for the transition from the old to the new mode of production and for economic and social progress to continue. This historical process – in which one mode of production, a more progressive one, succeeds another – continues until a classless communist society is established. We will then have a new era in the history of humankind.

6.

In this section we take up for discussion the stuff that Schumpeter himself puts into the 'black box' referred to earlier. This consists of his own theory of social classes and his modifications of the materialist method. The theory of social classes was presented by Schumpeter in a highly systematic way in an article entitled 'Social Classes in an Ethnically Homogeneous Environment'.¹³ But that is not the case with his modifications of the materialist method. These we find in some of his discussions of the actual historical processes, in particular of early European capitalist development. I have found it convenient to highlight these ideas – significant departures from Marx's way of thinking – by outlining (with 'desperate brevity', as Schumpeter himself would have said) the perspective from which he views early capitalist development¹⁴. In what follows, I will first outline leading ideas of Schumpeter's theory of classes; having done that I will highlight some of his ideas that we consider as his modifications of the materialist method.

I will start with a brief critique of Marx's theory of social classes from the Schumpeterian perspective. According to Schumpeter both the propertied and working classes are far more internally differentiated than Marx allows for in his analysis. For instance, small and medium-sized firms have interests that do not always, and necessarily, coincide with those of big

¹³ This is one of the two papers that make up the volume *Imperialism and Social Classes*. This paper was first published in 1927, the other paper in this volume, on imperialism, was first published in 1919.

¹⁴ Schumpeter's brief account of early capitalist development in Europe is included in his article 'Capitalism' in *Encyclopaedia Britannica*, 1946 edition, *History of Economic Analysis*, Part II, chapters 2 and 3, and the essay 'Social Classes in an Ethnically Homogeneous Environment'.

business. The same holds for farmers and the rentier class. Similarly, the working class is anything but internally homogeneous; there is little point in talking of a common class interest of an unskilled worker and a highly paid lawyer or accountant. Further, Marx's assumption that the capitalist class is internally stable, that there is negligible social mobility, is highly questionable. The fact that there are always industrialists and bankers on the one hand and property-less workers on the other gives the false impression that families within those classes are self-perpetuating and that entry into and exit from the upper strata of society are exceptional events. The questioning of these assumptions – the homogeneity of the two main social classes under capitalism and the internal stability of these classes - underlying Marx's schema has obvious and serious consequences for his theory of social revolution, a theory that crucially depends on the clash between the irreconcilable interests of the two protagonist classes.

If the phenomenon of social classes cannot be understood in terms of two classes based on the ownership and lack of ownership of means of production, how do we then explain it? In Schumpeter's theory the leading factor that accounts for the existence of social classes is the differences in aptitudes of individuals. Schumpeter defines aptitudes in terms of qualities such as the general level of intelligence, capacity for intellectual analysis, will power, resoluteness, ability to command obedience, etc. This means that specific talents, such as those of opera singers, do not play any part in his theory of classes. He is interested in qualities that make for social leadership, a leading idea in his schema, as we will see shortly.

The aptitude for leadership (or most aptitudes) is not confined to a select group in the population. Most of us have it in some degree. For instance, a school teacher could not function successfully without possessing it in some measure. Most of us have it, but some have it more than others.

Now we consider another important concept in this theory. This is that of social functions that the environment at any time makes 'socially necessary'. In any society of any size and complexity, there exist a variety of social functions that need to be performed. These functions have different social values. For instance, in feudal society the function of a warrior carries a much higher social value than that of ploughing the land; in capitalist society, a society whose primary orientation is towards economic activity, the introduction of new methods in the production system is given a higher social value than the work of an unskilled labourer. Although Schumpeter does not go into any detail on this point, we have here a clear idea of a hierarchy of social functions, and of the class structure consisting of a hierarchy of families located according to the social value of the functions they perform. And

the functions they perform depend on their aptitudes. Thus, people who possess qualities of leadership to a higher degree will occupy places in the upper strata of society, and those whose aptitudes are limited in this respect will find themselves in the lower layers of the social hierarchy.

Another important idea in the theory is that of social mobility. It is seen as ascent into, and descent from, the upper strata of society. Social mobility is assumed to be a feature of all societies, particularly of capitalism. We may say, with some exaggeration, that all that a peasant in the Middle Ages needed to rise in social hierarchy was the aptitude to distinguish himself on the battlefield (and of course to possess a horse and appropriate armour). With little or no exaggeration it could be said of the early period of capitalist development that it was people with 'extraordinary' qualities of leadership – entrepreneurship - who rose from the lower strata of society to become pioneers of capitalism, that is, who became merchants, bankers and craft guild masters. Similarly, under developed capitalism the barrier to ascent into the business class set up by lack of ownership of means of production (emphasised by Marx) is scaled with the help of bank credit.

Thus, class barriers are always in a state of flux. There are shifts of families within a class. These movements depend on the extent to which different families can solve the problems with which their environment confronts them. The qualities that enable a family to rise in its own class are the same that enable it to ascend into the upper strata. We thus have a picture of constant upward and downward movement: families with ability moving up the social hierarchy, and those who have lost the quality of leadership of their forefathers descending into the lower strata of society. Although Schumpeter does not put it in these terms, we can say that there is a long term tendency in historical time for the optimal allocation of abilities and aptitudes across the variety of functions that the changing environment creates. The upper strata of society are constantly replenished by new talent and, by the same logic, the lower strata are constantly denuded of it.

Aptitude for leadership may be inherited or acquired by the individual. Schumpeter takes no definite position on this question in so far his theories of classes and capitalist evolution are concerned. For this reason we do not need to pursue this question further. We do note, however, though only in passing, that to simplify his discussion of the class phenomenon he chose to neglect the factor of ethnicity. I think this simplification on his part does give an unambiguous indication that ethnicity (and therefore inheritance), in his view, did constitute a relevant factor in the distribution of abilities in society. But we must emphasise that whatever

position one takes on this question, the assumption of social mobility remains central to Schumpeter's theory of capitalist evolution.¹⁵

One implication of this theory may be immediately noted. Since in every society of any size and complexity there must be social classes (a result that follows from his definition of the class phenomenon), a socialist society could not be class-less. Furthermore, those with the exceptional qualities of social leadership, and who are ranked the highest in terms of their social value under capitalism, would have to occupy a similar position under socialism – if socialism is to be managed efficiently and if it is to survive as a social system. We see that Schumpeter's socialism seems to be very different from that of Marx's vision.¹⁶

So much for the theory of social classes. We will see presently how it informs Schumpeter's theory of capitalist economic development. Now let us note some important modifications to the materialist method as suggested by Schumpeter's interpretation of early capitalist development.

For Schumpeter economic development means capitalist development. Origins of capitalism can be traced back to the classical world, in fact further back to Hammurabi, if you like. There was then production on private account aimed at the market; there were merchants who traded locally and internationally, and there were bankers to whom producers had access. The capitalist enterprise did not totally disappear in the Dark Ages. And the warrior society (feudalism) that emerged from the disorders of the time contained within it practically all the significant elements, either lingering from the Roman times or recently formed, of capitalism. By the eleventh century, alongside the evolution of feudalism, a class of definite bourgeois character had made its appearance. By the beginning of the thirteenth century, when the feudal civilisation was reaching its zenith, the bourgeoisie as a class was already outgrowing the feudal institutional framework. By 1500 many of the phenomena that we associate with modern capitalism had made their appearance. The economy continued to develop on capitalist lines, but the political frame of society remained stubbornly aristocratic. The descendants of the old warrior class continued to be the pivot of the social system.

¹⁵ To get some idea of Schumpeter's thinking on the question of inheritance and 'racial' theories, see *History of Economic Analysis*: 788-89. Some readers may find it interesting that he considers Sir Francis Galton, the eugenicist, as one of the three greatest sociologists, the other two being Vico and Marx.

¹⁶ Schumpeter sees socialism as culturally indeterminate; he defines it wholly in terms of public control (unspecified) over means of production, and production carried on public rather than private account. In Marx's vision socialism means the entire structure of production being under the control of direct producers and the society organised in such a way that the full development of every individual is its governing principle.

According to Schumpeter this symbiosis between two different 'social systems' (or two distinct social classes) prevailed up to the middle of the eighteenth century. This latter development he attributes to certain external (external to the logic of capitalism), incidental factors, in particular to the flow into Europe from the New World of large quantities of gold, and the breakdown of what he calls 'medieval internationalism', the dual power of the Holy Roman Empire and the Catholic Church.¹⁷ What emerged was the Nation State or Absolutism. This, according to Schumpeter, was feudalism run on capitalist lines. The King's position remained essentially feudal, but the state shaped economic policy to propel capitalist development (Mercantilism)¹⁸, and the king and the aristocracy lived increasingly on the revenue generated by capitalist development. Over time, the descendants of the old warrior-aristocratic class metamorphosed themselves into statesmen and administrators, diplomats, colonial officers, and so on. Having lost one social function (war), they had found another one (public administration).¹⁹ This symbiosis was the essence of the Nation State. And not only of that. This arrangement (England here is the 'classic' case) came down right into the nineteenth century.²⁰

Two points are of particular interest here. First, capitalism as a mode of production (that is, production on private account aimed at the market and availability of credit) pre-dates feudalism. And its development is one of 'slow and continuous transformation' going back to the time of the emergence of feudalism.²¹ This means that theories that attempt to explain the origins or 'rise' of capitalism in Europe by appealing to some special factor (such as the rise of Protestantism in the sixteenth century) are explaining a problem that simply does not exist. The same criticism applies to Marx's theory of 'primitive accumulation' that placed the evolution of capitalism in Europe from around the last part of the fifteenth century.

Second, we note here an interesting modification of the materialist method: a disjunction between the economic base and the superstructure. We have seen that in Schumpeter's

¹⁷ *History of Economic Analysis*: 144-47.

¹⁸ It may be noted in passing here that what gives unity to the economic writings and debates of this period (roughly from the middle of the 16th to the middle of the 18th century) which are generally referred to as the 'school' of Mercantilism was that they were all concerned with the economic problems of the Nation State and economic development.

¹⁹ *Capitalism, Socialism, Democracy*: 163.

²⁰ Marx also subscribed to the idea of a 'symbiosis' (in England) between the bourgeoisie and the landed aristocracy, though with a different slant on the nature of the relationship. In an article titled 'Tories and Whigs' published in the *New York Daily Tribune* (11 September 1852) he referred to the Whigs as 'the aristocratic representatives' of the bourgeoisie. In an article written for the German newspaper *Neue Oder-Zeitung* (6 March 1855), with the title 'The British Constitution', he expressed the view that the bourgeoisie was (before the 1832 Reform Bill) the ruling class 'in actual practice' and the aristocracy formed the 'official government'. After the Reform Bill, the bourgeoisie was 'on the whole acknowledged also *politically* as the *ruling class*', but that it was 'on the condition that the entire system of government in all its detail ... remained safely in the hands of the landed aristocracy.'

²¹ 'Capitalism', article in the *Encyclopaedia Britannica*, 1946 edition.

interpretation of early capitalist development though the economic base continues to increasingly become capitalist, the political structure remains obstinately pre-capitalist. What is more, the pre-capitalist political structure endured into the post-Industrial Revolution period, and survived right up to the end of the nineteenth century. It is a general position of Schumpeter that elements of the superstructure – political institutions, social structure, socio-psychological dispositions of people, etc., – are coins that do not melt easily and that this historical lag between the economic base and the superstructure plays a fundamental part in the evolution of capitalism.

We must emphasise, however, that this idea constitutes a modification of the Economic Interpretation of History, not its rejection. The feudal superstructure did not arise autonomously; it arose in response to the material conditions of life and to serve the vital needs of society. But once firmly established it – or some elements of it – tended to persist for a time even though it had lost its original function. However, it will change as the economic conditions and the vital needs of society change and eventually come into line with the economic base. I think Marx would not have disagreed with the idea that there will be a time lag in the adjustment of political structures to economic conditions, but this idea plays no role in his system. The idea that a lagging superstructure continues to play an important role in social evolution is unique to Schumpeter and as we will see in section 12 below it is an essential part of his overall schema.²²

7.

A number of times in the course of our earlier discussion we had occasion to refer to the 'internal necessities' that cause economic change to take place. It is now time to explain what these 'necessities' are. We will start with Marx. But before we outline the nature of these 'necessities' we remind ourselves that although Marx stated his materialist method as a general hypothesis that was supposed to hold for all modes of production, it was only in the case of capitalism that he actually attempted to construct a theory of its functioning and evolution.²³ Thus, the task he set himself in the writing of his *Capital* was, in his own words, to discover the 'laws of motion of capitalism' (not of the human society in general). It is therefore to Marx's discussion of capitalist development that we now turn. So the question to be discussed is: What are the 'internal necessities' that drive capitalist development? These

²² This idea plays a central role in Schumpeter's theory of imperialism (according to which imperialism in the age of capitalism is atavistic in nature). It was presented as an alternative to the neo-Marxian theories of imperialism that were being advanced at the time. See his essay 'Imperialism' in *Imperialism and Social Classes*.

²³ Ten years after the publication of the first volume of *Capital* he disclaimed the suggestion that he had tried to produce a 'historical-philosophical theory of the general path of development prescribed by fate to all nations whatever the historical circumstances they find themselves in'. He indicated that his main objective had been to understand the development of capitalism. See his letter to *Otyecestvenniye Zapisky*, a Russian newspaper.

'necessities' according to Marx arise from the very nature of capitalism; they arise from its internal logic that is unique to this mode of production. It thus becomes crucially important to understand the manner in which Marx conceptualises capitalism.

In identifying the main features of capitalism, Marx used some of the ideas of his classical predecessors. Adam Smith, for instance, had conceptualised the emerging 'commercial society' of his time as one in which there are owners of 'stock' (capital) who want to put 'industrious' people to work in order to make profit; and there is a class of people who, lacking their own means of subsistence, need a 'master' for whom they can work for a wage and thus make a living. Adam Smith had also drawn attention to another feature of modern capitalism. This he called the principle of natural or perfect liberty. By this he meant the freedom of the capitalist to choose his field of investment and the freedom of the worker to choose his occupation and employer. Marx's definition of capitalism embodied all these three features.

Thus, the capitalist mode of production is characterised by, first, the accumulation of capital in the hands of a small class of profit-motivated people, second, the existence of a large class of property-less people who are forced to sell their labour-power on the market in order to survive and, third, competition in the sense of free mobility of capital and labour in the economy.²⁴

We should add a further condition for the existence of capitalist production, which though implicit in what has been said above should be made explicit. According to Marx, it is a necessary condition for capitalist production to come into existence that the unit of production is large enough for it to practice division of labour and realise economies of scale. (For Marx, the production in the medieval guild, though motivated by private profit, is not capitalistic, but that in the pin factory of Adam Smith's famous illustration is. The latter practises division of labour and enjoys economies of scale, the former does not.) In the absence of economies of scale – a situation in which large-scale production enjoys no advantage over the small scale – there could be no capitalist production, and there could be no capitalist class. Such a world will be one of independent producers, not of a small class of capitalists and property-less labour; in it every one will be able to set up his own production.

²⁴ These are in fact the three conditions for the emergence of the capitalist mode of production - to repeat, a small capitalist class that has ownership of society's means of production and subsistence; a property-less working class that has been appropriately disciplined to work under changed conditions of production (from agriculture to modern industry), and juridically free labour and free capital mobility. His entire discussion of 'primitive accumulation' in *Capital*, vol.1, is aimed at showing how these conditions came to be met historically in Western Europe (England being the classic case).

In such a world there will also be no possibility of sustained, cumulative development that is an essential feature of capitalism.

A number of points should be noted. First, it is only under the conditions outlined above that labour-power becomes a commodity – it is bought and sold like any other commodity under conditions of free competition, a unique feature of the capitalist mode of production. Second, in the way that Marx defines capitalism, the concept of ‘capital’ assumes a very specific meaning. Of course, every society has capital in the sense of buildings, tools, etc. But capital under the capitalist mode of production comes to assume an altogether a different form. This capital is moveable (footloose, as we might say today), that is quite unlike guild capital that was tied to the master’s craft or the tools, etc., owned by a peasant. This capital seeks new avenues of investment and new markets; it seeks self-expansion. We note also that this capital carries with it a relationship of economic and social power – the capitalist class possesses all the means of production and subsistence and therefore can, even under conditions of free mobility of labour, exercise power over the working class. Third, the capitalist mode of production makes for maximum efficiency. Profit seeking is combined with concentration of productive resources and therefore realisation of economies of scale, and competition. The latter provides a mechanism of resource allocation. Under changing conditions capital and labour must move from less to more productive activities. If capital does not move, the owner-producer will be eliminated from the market; if labour does not move, it will become unemployed and starve.

Having identified the nature of capitalism, we can begin to answer the question regarding the ‘internal necessities’ driving economic development. Marx’s capitalist is quite unlike his counterpart in the orthodox theory. In the orthodox view the capitalist (like every economic agent) is essentially a consumer. He saves and invests to consume another day; that is, in the act of saving and investing he foregoes consumption today in favour of larger consumption in the future. He is under no *necessity* to save and invest. By contrast, in Marx’s model, the central feature of capitalist production is the process in which the capitalist starts with a certain sum of money (M) that has been previously accumulated, purchases commodities such as raw materials and labour-power (C), which labour converts into commodities and which are typically sold for a sum (M’), where (M’) is greater than (M). The difference between (M’) and (M) is the surplus value which arises from the fact that labour produces a value that exceeds the value of all the inputs used up in production and the value of labour-power and that the capitalist can somehow appropriate it. This is the source of the capitalist’s profit.

We can now see why Marx's capitalist must invest the surplus appropriated by him (after allowing for his consumption). He must do this because he lives in a highly competitive environment in which his position is constantly under threat from other capitalists. To protect his position – to remain a capitalist – he must invest to improve his methods of production and the quality of his products; he must invest to enlarge his scale of operations, achieve greater efficiencies, find new markets, and so on. He must increase the surplus value that he appropriates and amass more and more capital (and in the process drive smaller and less efficient capitalists to the wall). The inner necessity of development lies in the institutional frame of capitalism, in the flesh and bones of which this mode of production is made. Just as the knight of the Middle Ages lived by physical combat and war, the capitalist lives by pursuing the profit-accumulation motive.

So much for the 'inner necessities' that determine capitalist behaviour. Now a few words how this behaviour results in sustained economic development. According to Marx, early capitalist development²⁵ from, say, 1500 to the middle of the eighteenth century (here, as elsewhere, England is the 'classic' case) laid the foundation for the establishment of the modern power-driven industry, the emergence of machine building as a specialised activity, and the establishment of the industry's capacity to harness natural science to production. In this way, under modern capitalism, rising productivity of resources (appropriated by the capitalist as surplus value) becomes the basis for accumulation and economic expansion. The scarcity of land presents no barriers to expansion, as it did in Ricardo's model. The application of natural science to agricultural production holds the operation of the law of diminishing returns in permanent abeyance. Thus, the system creates its own material resources for expansion.

The supply of labour also presents no barrier to expansion. Marx argues that normally employers will face an elastic supply of labour over time. This is made possible by natural increases in population, the existence of traditional economic activities which contain a large reservoir of under-utilised or less productive labour on which modern industry can draw (without significantly raising wages), and the increasing mechanisation of production that 'saves' on labour.

²⁵ According to Marx's periodisation of the process of early capitalist development in Europe, 'primitive accumulation' begins during the second half of the fifteenth century and from the sixteenth century goes hand in hand with the 'system of manufacturing'. The latter is a form of industrial organisation that stands between the craft technology of the medieval guild and the power-based industry that developed with the Industrial Revolution. The 'putting-out' system was an aspect of the 'manufacturing system'.

Finally, as we have already noted, the institutional frame of capitalism enforces competition. Business survival depends on doing as well as the best of your competitors. In this way constant improvements in the techniques of production become a way of business life.

The conclusion must be that once the economy has made the critical breakthrough from craft technology of the feudal period to power-driven industry, and from the restrictive frame of guild production to free competition, it becomes characterised by virtuous circles of technical progress, high productivity and high rates of accumulation. It comes to be characterised by self-generating and self-sustaining expansion, or what a later generation of development economists would refer to as the process of cumulative causation.

8.

This completes our discussion of Marx's theory of *economic* development. The second part of Marx's project consists of showing that economic change leads to social changes, more specifically, that economic development will ultimately result in the demise or breakdown of capitalism and the establishment of a socialist order. As the general features of this aspect of Marx's thought – economic change leading to social changes – were discussed earlier (section 5), here we can be brief. The core of the argument in the present context is that through the working of its internal logic capitalism will reach a stage in its economic development that no further progress within its institutional frame will be possible. But this failure will not leave a void or result in chaos. Through its own logic it would have, in the course of its development, completed all the essential requirements for the successful establishment of its successor mode of production. The method of dealing with these issues followed from Marx's general evolutionary approach according to which the future is being formed in the womb of the present. This approach suggests that if we can understand the present (by understanding the internal logic of the system) we can understand the direction that development will take in the future. Thus, Marx sought to identify certain tendencies in contemporary capitalism that arise from its internal logic and to project their working into the future. It is these tendencies that he referred to as the 'laws of motion' of capitalism.

Now there are at least two difficulties with this method – if we treat it as providing a prognosis or prediction of future course of events rather than as a framework for considering various possibilities. One difficulty is that the logic of capitalism does not give an unambiguous indication of the direction that Marx's 'laws of motion' of capitalism will take. This is the case because these tendencies are themselves made up of other tendencies which can pull in opposite directions. Without going into any detail we note that the tendency of the rate of profit to fall (Marx's 'tendential fall of the rate of profit') is made up of the

tendency of the organic composition of capital (the ratio of capital costs to labour costs of production) to rise, and the forces determining the ratio of surplus value to labour costs. The tendency of the organic composition of capital to rise is itself made up of a variety of forces that can go in opposite directions. To his credit, Marx fully recognises this problem, for we see that his chapter on the law of the tendential fall in the rate of profit²⁶ is immediately followed by a chapter entirely given to a discussion of factors that may counteract the tendency for the rate of profit to fall. These he refers to as 'counteracting factors'. But his treatment of this problem is rather arbitrary: he distinguishes between 'tendencies' and 'counteracting factors' and claims that 'tendencies' are made up of forces that dominate historically, while 'counteracting' factors, though operative, are unable fully to offset the effects of 'tendencies'. What are 'tendencies' and what are 'counteracting factors' is a question that can only be judged with reference to actual experience. It seems to us that the logic of capitalism (even in Marx's own theoretical framework) does not work unambiguously in a pre-determined direction.

The other problem with Marx's method (to repeat: if we treat it as making predictions) refers to the role of factors that are external to the logic of capitalism in determining the course of historical development. Such factors, fortuitous and unpredictable by their very nature, may alter the course of events as indicated by the working of the tendencies inherent in capitalism. Schumpeter, who adopts a method similar to that of Marx – that is examining present-day tendencies to see in which direction they might lead – places a particular emphasis on the role of external factors. Qualifying his own prognosis of capitalist development, he writes²⁷:

Any prediction is extra-scientific prophesy that attempts to do more than to diagnose observable tendencies and to state what results would be if these tendencies should work themselves out according to their logic. In itself, this does not amount to prognosis or prediction. Factors external to the chosen range of observation may intervene to prevent that consummation; because with phenomena as far removed as social phenomena are from the comfortable situation that astronomers have the good fortune of facing, observable tendencies, even if allowed to work themselves out, may be compatible with more than one outcome, and because existing tendencies, battling with resistances, may fail to work themselves out completely and may eventually 'stick' at some half-way house.

²⁶ *Capital*, vol. 3, chapter 14.

We conclude first, that it is doubtful if Marx's model of capitalist development can be taken to suggest a logical necessity for it to take one particular direction, and second, that such logical necessity can not be trusted to translate into historical necessity.

There is another difficulty, of a different kind, with Marx's method. Marx's entire theoretical argument on the necessities that drive capitalism toward self-destruction rests on the assumption of a 'closed economy' in the sense that the capitalist system is seen as confined within the borders of a single nation. Now, this assumption is necessary when we are, as a first approximation, trying to understand the manner in which capitalism functions. But we know (from Marx's own argument) that the 'inner logic' of capitalism (when we see it as confined to one country) propels it across its national borders; that capitalist producers in one country set out to find new investment opportunities, new markets for their products, etc., in other countries. In other words, as already noted, it is an inherent tendency of the capitalist mode of production to cross its national boundaries to become a world-system. This means that any results obtained from a model that assumes a 'closed economy' would, to make them applicable to the real world, need substantial extension. The future of capitalism, since it has the inherent tendency to become a world-system, needs to be discussed (to use the language of *The German Ideology*) in the 'world-historical' context,²⁸ that is, as a world-system. Marx was of course not able to extend his analysis in this direction. In fact, as we see in the next section, Marx was not even able to complete his analysis of the capitalist process as a whole even in the context of the 'closed economy'.²⁹

9.

We now turn to Marx's discussion of the future of capitalism. We see that there are two strands in this discussion. The first, as already noted, relates to the idea that during the process of capitalist development preparation for the establishment of socialism has been going on – the new mode of production has been, as it were, growing within the womb of the old. The second addresses the question of the eventual disruption of capitalism. Thus, the ripening of the conditions for the social management of production under socialism and the

²⁷ *Capitalism, Socialism and Democracy*: 422; see also p. 61.

²⁸ We see that in the very first statement of the materialist method, Marx (writing with Engels) emphasised what we may call the international dimension of this method. See *The Germany Ideology*, pp.50-75. This emphasis, as noted earlier, is repeated in *The Communist Manifesto*. The 'neo-Marxian' theories of imperialism that started to be published from the early years of the twentieth century may be seen as attempts to extend Marx's theoretical analysis of capitalism beyond the confines of a 'closed economy'. See for instance, R. Hilferding, *The Finance Capital* (1910), Rosa Luxemburg, *The Accumulation of Capital* (1913) and V.I. Lenin, *Imperialism* (1916).

²⁹ Marx had planned to include in his work discussion of international division of labour, colonies, international trade, and 'world markets and crises'. His research project thus went well beyond what he was able to deal with (though incompletely) in the three volumes of his *Capital*. See his letter to F. Lassalle dated 21 December 1857.

process of disintegration of capitalism have been proceeding apace. We will start with the first strand.

First, it is a necessary condition for the establishment of a classless, socialist society that there should be abundance of material goods. According to Marx, you cannot create a classless society in a poor country; people will fight over scarce goods with the result that classes (in one shape or another) and economic and political domination will re-emerge. Socialism can only be established when society has attained the potential to produce abundance of material goods. It has been the historic function of capitalism to lay the basis for such capacity, at least as a potentiality. This was in the course of being achieved through a long process of accumulation and by the harnessing of natural science to the needs of production.

Second, another necessary condition for socialism is that society's productive resources are concentrated in large units. Social management of resources cannot be effective when resources are dispersed in small parcels over a large geographical area (as in a society of small peasant holdings). Capitalist development was fulfilling this condition by achieving concentration of production in large units. This development, as we have seen, arises from the fact that under conditions of technical progress there are no limits to the increase in the size and efficiency of the production unit.

Third, concentration of productive resources in large units as well as the geographical agglomeration of related industries (that necessarily goes with economic development) means, of course, large geographical concentrations of workers. Concentration of large numbers of workers, broadly doing similar types of work, sharing the same working conditions and the same problems, provides the foundation for the formation of class-consciousness – consciousness of the identity of economic interests. (Because of their wide geographical dispersion, peasants are seldom able to achieve class-consciousness, despite their identity of interests.) This leads to collective action to improve their working conditions. Through these struggles workers come to see that their salvation lies only in the overthrow of the existing system. (Marx was aware of the increasing differentiation within the working class, but decided to treat it as merely a 'counteracting factor'.)

Let us now, finally, try to convey some idea of Marx's theory of the 'breakdown' of the capitalist system (or, rather of recurrent economic crises). It must be said straightaway that in this vital aspect of Marx's project his theory is far from complete. As Schumpeter put it, it is an 'unfinished chapter' of his work. It is presented in that part of *Capital* (volume 2) that

Marx was unable to complete.³⁰ Engels who was left with the task of editing the second and third volumes of *Capital* said that Marx had left a 'large number of versions [of volume 2], most of them incomplete'.³¹ The following two paragraphs are intended to give some indication of the complexity of Marx's thinking on the subject of economic crises.

The principal contradiction in the capitalist system is between the society's capacity to produce and the capacity to consume, the latter being limited by the maldistribution of the social product between profits and wages. This is the root cause of economic crises that characterise capitalist production. There are tendencies in the economy, in particular the tendency toward increasing mechanisation, that create the tendency towards chronic unemployment that keep wages down practically at the subsistence level. This restricts the consumption of workers who constitute the mass of the population. The restriction of the output of consumption goods industries means that the demand for capital goods will also be restricted. This means in turn that investment in capital goods industries will not expand sufficiently to absorb the potential output of these industries. Thus, the conditions that keep wages (and therefore consumption) down set the chronic tendency for the failure of the system to realise its potential with respect to production. Hence, economic crises that Marx claimed would get worse and worse with time. To quote Marx here: 'The ultimate reason for all crises always remains the poverty and restricted consumption of the masses, in fact of the drive of capitalist production to develop the productive forces as if only the absolute consumption capacity of society set a limit to them'.³²

However, this is not a problem that can be resolved by government policy, say, aimed at raising wages in order to boost consumption. In the second volume of *Capital* (pp.486-87), Marx observes that it is a 'pure tautology' to say that crises are caused by a lack of effective demand. He writes: 'If the attempt is made to give this tautology the semblance of greater profundity, by the statement that the working class receives too small a portion of its product, and that the evil would be remedied if it received a bigger share, i.e. if its wages rose, , we need only note that crises are always preceded by a period in which wages generally rise, and the working class actually does receive a greater share in the part of the annual production destined for consumption.' But this improved situation of the working class does not avert the crisis. In fact, the relative prosperity of workers is always a 'harbinger of crises'.

³⁰ In fact, Marx's ideas on economic crises are to be found in all the three volumes of *Capital*, his *Theories of Surplus Value* (three volumes), and other writings.

³¹ See Engels' editorial 'preface' to *Capital*, vol. 2.

10.

We turn now to Schumpeter's theory of economic evolution. Schumpeter takes as his starting point the Walrasian model of a stationary (capitalist) economy in perfect equilibrium. He observes that in this model there are three 'factors', treated as data or parameters, through which change may be introduced into the economy. These are consumer tastes, quantities of factors of production, and methods of production or technology. Schumpeter excludes from his own model the first two as possible independent sources of change. Changes in tastes seldom occur autonomously. In any case, given the level of consumer incomes and production methods (as assumed in Walras' model), any change in consumer tastes will result in a reallocation of society's existing resources rather than initiate a process of 'incessant change'.

Changes in factors of production can be divided, broadly speaking, into changes in population and produced goods. Schumpeter has little difficulty in dismissing the first as an independent factor in initiating economic change. He argues that there is no unique relation between increase in population and, say, increase in output per head: population changes may be associated with falling, constant or rising levels of productivity. Increases in produced goods if they embody the same technology as that already in use, say, production of more and more mail coaches, can also not initiate a process of incessant change. In other words, accumulation of capital by itself does not necessarily mean development.

This is how in Schumpeter's model the entire burden of explaining economic development falls on autonomous changes in methods of production - a term which he uses broadly to include not only changes in techniques narrowly defined, but also new methods of business organisation, new products, discovery of new materials and markets. He calls these changes 'Innovations'. The essence of the idea is that things are done differently from existing practice and as a result *existing* resources are put to better and more productive uses. We note that since innovations do not take place by themselves, they have to be introduced by some one, that 'some one' comes to take the central place in Schumpeter's theory of development. He or she is the Entrepreneur.

Let us now see how entrepreneurial initiative generates economic development.

We start (following Schumpeter) with a competitive capitalist economy in the stationary state and imagine that an entrepreneur enters upon this scene with a plan to introduce an

³² *Capital*, vol 3, 615

innovation (say, a new method of production).³³ We assume that the innovation is a major one, say, like the railways or the computer (rather than a new kind of sandwich), and that it is financed by bank credit. Let us now see the sequence of events that follows.

The success of the innovation will mean that the entrepreneur introducing it will have seized an advantage in terms of costs over his established rivals. With the old price still prevailing he will enjoy 'monopoly' profits the size of which will be determined by the difference between his costs and those generally prevailing in the industry and the time it will take others to match his efficiency. After a certain time, as the success of the new method is perceived, some of the established firms will begin to imitate the new method and follow the path cleared by the leader; and as the success of the new method is more widely observed more and more will follow suit. Eventually, the generality of the producers will have adopted the new technique. By then price of the product will have fallen to the average costs of production (associated with the new method) and profits will have been eliminated. This dynamic process, we may note in passing, is sometimes referred to as 'Schumpeterian competition'.

We can now summarise some of the results of the changes brought about by the innovation in the industry where it was introduced. (a) Costs of producing the product in question have fallen and so has the price of the product; (b) The size of the market for the product in question should have increased (depending on its elasticity of demand) and, given the assumption of increasing returns to scale, we expect the typical size of the industrial unit to have increased; (c) most of the firms in the industry have earned profits, the size of profits of each firm depending on the stage at which it adopted the new method; (d) those firms that were unable to adjust to new conditions have been eliminated.

This is of course only a partial view of the process generated by the innovation in question (let us call it 'primary' innovation). It is partial because up to this point we have only considered the impact of the innovation on the industry where it was first introduced. Seeing beyond it, we observe that the success of the primary innovation will naturally have an influence on other industries in the economy. There will obviously be a significant impact on the sectors that supply it with capital goods and other inputs. This impact will in the first instance consist of increased demand for their products. And this in turn will increase the

³³ Schumpeter defines a capitalist economy as one in which, first, means of production are privately owned and, second, production is motivated by private profit. He adds: 'But, third, the institution of bank credit is so essential to the functioning of the capitalist system that, though not strictly implied in the definition, it should be added to the two other criteria.' See his article 'Capitalism' in *Encyclopaedia Britannica*, 1946. This third criterion is crucial for Schumpeter's entire argument, as we will see as we proceed.

possibilities for greater division of labour and general technical improvements in these sectors of the economy. Downstream industries will also be expected to receive developmental impulses from the primary innovation. The new technology associated with the primary innovation (and the 'secondary innovations' that may have followed) might also have found uses in other sectors of the economy. The general point here is that an important innovation in one sector of the economy gives rise to chain reactions and creates possibilities for development well beyond the field of its original application.

This view of the process suggests *clustering* of innovations in a small number of related sectors. Innovations will also be clustered in time. It is at this point that Schumpeter's theory of development links up with his theory of the business cycle. which, as we will see presently, is simply an aspect of the development process. What we have been witnessing in the preceding paragraphs is an economic upswing or a period of prosperity initiated by the primary innovation. This phenomenon is explained by the fact that innovations and developments associated with them come in a swarm-like movement. First comes the leader, the original innovator, who is followed by his imitators in the same industry; then, we see entrepreneurs introducing secondary innovations in other parts of the economy who are then followed by *their* imitators, and so on. It is this herd-like stampede that causes the upswing.

The period of prosperity *necessarily* comes to an end and is followed by a period of recession. A recession is a reaction to an upswing; it is a time for adjustment after a period of technological and industrial upheaval; a time to absorb the results of the developments initiated by the primary innovation. If there were no clustering of innovations, that is, if innovations were introduced independently of each other and distributed randomly in time, then, in those conditions, changes associated with them would be gradually and smoothly absorbed by the system. If innovations were always of the type represented by a new type of sandwich, then also new changes would be smoothly absorbed in the economy. (And of course there would be no technological revolutions that have characterised modern development.) The phenomenon of the business cycle then would not exist, though there would still be good times and bad times for reasons external to the economy. But when innovations are major in magnitude and are bunched in time then the changes initiated by the primary innovation cannot be smoothly and gradually absorbed in the system. There is then the problem of the economy absorbing these changes. The absorption of a concentration of innovations and their consequences (for instance, restructuring of large parts of the economy, elimination of inefficient businesses, transfer of labour from contracting to expanding industries, liquidation of indebtedness incurred during the upswing

through inflationary finance, and so on) requires a period of calm. And that is provided by the recession. The trough of the recession represents the economy's new equilibrium. The re-establishment of equilibrium shows that the upheavals created by the introduction of the innovation eventually correct themselves.³⁴

The sequence of events from one position of equilibrium to the next, in historical time, constitutes the process of economic development. During this interval, the economy undergoes a number of important changes. Some of these may be noted. (a) As a result of entrepreneurial initiative profits emerge in the economy; these are unequally distributed among businesses, generally leaders earn more than the 'mere imitators'. (b) There is increase in labour productivity and aggregate social product. (c) The composition of the social product changes significantly. (d) Industry structure is transformed; it is characterised, among other things, by the emergence of new industries and increase in the size of the typical unit. (e) The technology used in various sectors of the economy improves significantly. (f) There is an increase in the real incomes of consumers since all improvements in labour productivity and cost reductions are passed into lower prices.

Finally, two interesting features of Schumpeter's theory should be noted. First, we observe that though recession is a necessary reaction to the upswing, the reverse is not true. The upswing does not automatically follow a recession. There is no automaticity in the process of development. The next period of prosperity (and continuation of the development process) must now wait for a new act of business leadership, the introduction of a major innovation. We will expect activity to resume, assuming that the spirit of capitalist enterprise is alive. But since the introduction of innovation is a matter of individual volition its timing cannot be predicted.³⁵ Second, an act of previous saving has not figured in the outline of the model presented above. (Recall that the primary innovation was introduced with the help of bank credit.) The essence of the development process lies in the use of existing resources more efficiently, their diversion from less to more productive uses. In fact, as we will see presently, the phenomenon of savings is neither a necessary nor a sufficient condition for development.

³⁴ We note the following points in passing: (a) The factors such as deficiency of aggregate demand which concerned Marx, and later Keynes, so greatly have no place in Schumpeter's explanation of the business cycle. (b) Since the business cycle is part of the natural process of economic development there is no room here for government intervention to 'mitigate' the effects of recessions. (c) Recessions that we are talking about here are distinct from depressions of the type experienced during 1929-33. The latter represent a pathological phenomenon that is explained differently and may require intervention.

11.

It will be apparent from what has been said so far that there are important similarities between certain aspects of the theories of Marx and Schumpeter.³⁶ For instance, for both innovation or 'constant revolutionising of methods of production' - a process in which the new constantly destroys the old - lies at the heart of economic development. For both development is associated with concentration of industry and tendency for the typical size of the manufacturing production unit to increase. It will be noted that these similarities arise from their method, which suggests that the economy should be seen in organic terms, that is, in the relatedness and interdependence of its various parts, and from the assumption of economies of scale. But there are also differences and these are of fundamental importance. In this section we further reflect on them.

We have seen in an earlier section that in Marx's schema the 'compelling motive' behind the pursuit of surplus value is its re-conversion into investment or accumulation. This is not just a matter of personal predilection; the capitalist is under a necessity to appropriate as much surplus as he can and to channel it into accumulation. The focus is entirely on the nature of the system, in particular on class behaviour, to the exclusion of individual volition. By contrast, in Schumpeter's discussion the focus is entirely on the individual - the individual who commands exceptional qualities of leadership. He is set apart from other members of his class who can at best only achieve efficient administration of resources within the frame of existing practice. The class phenomenon does not figure here at all.

Now, it must be obvious that Marx is not saying that the capitalist class acts collectively or in concert. It is apparent that if we start our consideration of the development process at one point in time (as Schumpeter does when he starts his exposition from a position of stationary equilibrium) one individual will be *seen* to take the lead and others will be *seen* to follow; and the leader will reap the reward of being first in the field with a new idea. Marx is fully conscious of this dynamic process and he gives a clear and explicit statement of what we earlier referred to as 'Schumpeterian competition'. For instance, he writes.³⁷:

Hence, the capitalist who [first] applies the improved method of production appropriates to surplus value the greater portion of the working day, than the other capitalists in the same trade. He does individually, what the whole body of capitalists

³⁵ Note that Schumpeter's model of the business cycle does not suggest periodicity in the sense of a constant period between troughs of the recession.

³⁶ For a discussion of such similarities, see J. E. Elliott, 'Marx and Schumpeter on capitalism's creative destruction: A comparative restatement, pp.45-68.

³⁷ Capital, vol 1:318-9 (Aveling and Moore edition, 1970).

engaged in producing relative surplus value do collectively. On the other hand, however, this extra surplus value [the leader's monopoly profit] vanishes, so soon as the new method of production has become general, and has consequently caused the difference between individual value of the cheapened commodities and its social value to vanish.

But Marx sees the introduction of innovations as a continuous social process in which at one time one capitalist will introduce a new method, at another some one else. The 'leader' is part of the on-going social process; he uses the contributions of others before him, and the 'mere imitators' may play just as important a role as the 'leader' when they disseminate the new idea and perhaps modify it and put it to different uses. There is no need to deny that individuals differ in their abilities; no need to see the capitalist class composed of homogeneous creatures. But Marx takes the view that to understand the essence of capitalism and its development we can neglect such differences and postulate what we may call typical capitalist behaviour - behaviour dictated by the market, the system. We can then attribute the 'revolutionising of the methods of production' to the bourgeoisie in general rather than to exceptional individuals.

Schumpeter directly confronts this 'automatism of accumulation' which suggests that accumulation takes place on its own accord, without the intervention of the 'subjective' or human factor. He writes.³⁸

Manifestly, the captured surplus value *does not invest itself* but must *be invested*. This means on the one hand that it must not be consumed by the capitalist, and on the other hand that the important point is *how* it is invested. Both factors lead away from the idea of objective automatism to the field of behaviour and motive – in other words, from the *social 'force'* to the *individual* – physical or family; from the *objective* to the *subjective*. It may be objected that the logic of the situation forces the individual to invest his profit, that individual motivation is only a fleeting intermediate phase. This is true, as far as it goes, and must be acknowledged by any reasonable person. Naturally the individual psyche is no more than a product, an offshoot, a reflex, and a conductor of the inner necessities of any given situation. But the crucial factor is that the social logic or objective situation does not unequivocally determine *how much* profit shall be invested, and *how* it shall be invested, *unless individual*

³⁸ J. Schumpeter, *Imperialism and Social Classes*:118-19.

disposition is taken into account. Yet when it is done, the logic is no longer inherent solely in the system as distinct from the individuality of the industrialist himself.

We note here that while emphasising the role of the individual and the subjective factor Schumpeter does not depart from the central tenet of the materialist approach. He is no Carlyle. He accepts the crucial importance of the 'social logic'. For him also the 'individual is a social fact'.³⁹ The point Schumpeter is making is that in any given situation (determined by the process of development that has gone before) there is a range of possibilities (perhaps a narrow range, but a range nevertheless) for further development. Which of these is chosen depends on the dispositions of the individuals concerned, the 'subjective factor'. The future shape of development (say, of a particular type of technology or even a revolution) is not uniquely determined by the social logic.⁴⁰

At this point we may wonder whether Marx would not have conceded the role that Schumpeter assigns to the individual (though, it must be added, Marx was not sympathetic to the notion of 'leadership'). But Schumpeter goes much further with this line of reasoning so that there can be no room for a compromise between the two viewpoints. While, Marx (as we have seen) neglects differences between individuals so that he can focus entirely on class behaviour, Schumpeter must highlight these differences to direct attention to the individual. What, in his model, the individual or the subjective factor does is to perform a *distinct* social function. It is distinct because it consists of doing new things that lie outside the limits of routine tasks that every one can perform. It requires for its performance exceptional qualities of leadership because social environment resists innovation or anything that is unfamiliar and untried. It requires (and we have here an assumption of fundamental importance for Schumpeter's model) a *special aptitude* that only a small fraction of the population possesses.⁴¹ The following passage makes clear the necessity of assuming that the aptitude for leadership is a *scarce* quality in society, and for this reason its possessor enjoys a special position in society and has to be appropriately rewarded⁴²:

Most members of the [business] class are handicapped in this respect [introduction of innovations]. They can follow suit only when someone else has already demonstrated success in practice. Such success requires a capacity for making

³⁹ Schumpeter rejects what he calls 'errors of individualism and 'psychologisation', distinctions such as 'individual vs the social', 'subjective vs. the objective'. *Imperialism and Social Classes*: 161.

⁴⁰ It will be noted that this observation is part of the larger question of 'the role of the individual in history', but we cannot go into that in this paper. Schumpeter's ideas on the subject are scattered in his *Imperialism and Social Classes* and *Capitalism, Socialism and Democracy*,

⁴¹ *Capitalism, Socialism and Democracy*:132

decisions and the vision to evaluate forcefully the elements in a given situation that are relevant to the achievement of success, while ignoring all others. The *rarity* of such qualifications explains why competition does not function immediately even when there are no outward barriers, such as cartels; and this circumstance, in turn, explains the size of the profits that often eventuate from such success. (Emphasis added)

We see here Schumpeter drawing upon his theory of social classes which stands in sharp contrast to that of Marx who sees capitalism entirely in class terms and the emergence of profit from the relationship between the two classes, a relationship of power and exploitation. In Schumpeter, there is no room for one class exploiting another. Profits (surplus value or exploitation) do not exist when the economy is in equilibrium. They emerge temporarily and exclusively as a result of entrepreneurial action. Schumpeter is of course aware that in real life a good part of investment comes from retained business earnings, but in his view increase of physical capital is an incident in the process of capitalist development, not its propeller. In the logic of capitalism savings (or surplus value) as noted earlier, are neither a necessary nor a sufficient condition for development. They are not a necessary condition because essentially development consists in doing things in new ways and in strict logic this can be done by diverting existing resources into uses that break with existing practice. And this in turn can be achieved through the institution of bank credit (included in his definition of capitalism). Previous savings (or surplus value) are not a sufficient condition for development because they can be used for doing things within the domain of existing practice - producing more and more mail coaches. The dynamic of the capitalist system - of which the *Communist Manifesto* spoke in such glowing terms - comes not from the bourgeoisie as a class, but from the creative spirits of exceptional individuals.

12.

Schumpeter said in several places that his prognosis – capitalism's 'march into socialism' – was the same as Marx's. But, given that Schumpeter's conception of capitalism is so different from that of Marx, it should come as no surprise that the mechanism of evolution suggested by him is very different from that of Marx. In Schumpeter's schema there is no economic breakdown and there is no impoverishment of the masses. On the contrary, long-term economic expansion raises the demand for labour which results in the improvement in its standard of living and increase in its social weight. Schumpeter's mechanism of social

⁴² *Imperialism and Social Classes*: 121. It will be noted that the idea that the aptitude for leadership is a scarce 'factor of production' and that its reward indicates its scarcity value has obvious neo-classical undertones.

evolution has to solve the apparent paradox of capitalism's economic success being associated with its political failure.

Before we proceed with our discussion of this question, it is necessary to say a word on Schumpeter's method of analysis. It will be noted that Schumpeter's method here is similar to that of Marx. It attempts to suggest a future course of development of capitalism on the basis of an examination of certain present-day tendencies in its working. But as already noted, Schumpeter was, unlike Marx, acutely conscious of the limitation of this method. He warned repeatedly that he was simply highlighting certain present-day tendencies and claiming no more than that if they worked themselves out in the future as they were at present the result would be as he visualised. We have also noted his view that a model of development could identify only those tendencies that were inherent in the capitalist process. But there could be – indeed, would be - factors external to the logic of capitalism, that could intervene and change the shape and form of social evolution as indicated by the present-day tendencies. Perceiving certain tendencies and visualising a goal on the basis of those tendencies is one thing, prediction is quite another.⁴³

It is with these reservations in mind that we now consider some of the tendencies that are generated by the very logic of the capitalist system and that seem to be taking it, despite its remarkable success in the economic sphere, towards its downfall. In what follows no attempt is made to present a comprehensive theory of the 'march into socialism'. Instead I will highlight some of the tendencies that I think are central to Schumpeter's thought.

It is a natural consequence of economic development under individualistic capitalism (that is, the form of capitalism in which the typical industrial unit is family-owned and family-managed)⁴⁴ that the size of the typical enterprise should increase. There is thus tendency for the emergence of giant, bureaucratic corporations that are characterised by separation of ownership and management. Typically, such an enterprise is owned by a large number of shareholders and managed by salaried executives. In this situation, the management of the enterprise comes under the control of committees or boards of directors, and scientific and technical research comes to be carried out by teams of experts. In this way progress becomes 'automatised' and 'institutionalised' and the individual entrepreneur, who was the principal actor on the stage of economic development, loses his social function. This has a profound effect on the bourgeoisie as a class.

⁴³ *Capitalism, Socialism and Democracy*. 163

We saw earlier that to start with the entrepreneur need not be a member of the capitalist class; the doorway to the capitalist class is open to men of extraordinary ability. It is this constant entry of men possessing qualities of leadership and willpower from other strata of society that gives the bourgeoisie its vitality as a class. As Schumpeter said in his *Theory of Economic Development*,⁴⁵ the bourgeoisie as a class is like a hotel, always full of people, but people who are forever changing, some coming and some going. It is this constant replenishment of its ranks by men of ability from other sections of society, and the exit of those who have lost the vigour of their forefathers who founded the enterprise, that gives the bourgeoisie as a class its dynamic character. With the evolution of the family-owned and family-managed enterprise into the giant corporation the bourgeoisie tends to lose its dynamism and then its social function – a function that consisted of taking the society technologically and economically forward. And, as we have already seen, a class that loses its social function tends to die (unless it is able to find another function). The social function is still there, but it is performed collectively rather than individually.

This process has important consequences for the institutional frame of capitalism. Here I will direct attention to only one of these – the weakening of the capitalist motivation or the ‘evaporation of the substance of property’. Under individualistic capitalism, the bourgeoisie worked primarily to invest. This sounds remarkably like Marx’s ‘Accumulate! Accumulate!’ We saw earlier that while in Marx this self-denial originates in the imperatives of the system, in Schumpeter the urge to invest is rooted in motivations of a personal nature – a sense of achievement, founding an industrial dynasty, providing for one’s children and grandchildren, and so on. And through this personal fulfilment the bourgeois performs a social function; he serves the long-term interests of society.⁴⁶ However, with the decline of individualistic capitalism the personal and family motivation tends to fade away. The businessman develops the psychology of a salaried executive, who is with one firm today and with another tomorrow. He loses the long-term perspective and the sense of commitment and responsibility that goes with ‘full-blooded’ ownership. Under individualistic capitalism the bourgeois would stand at the doorstep of *his* factory and defend it against attack. Would the salaried executive do the same? Or the ‘absentee’ shareholder?

⁴⁴ Schumpeter uses the terms ‘Intact’ and ‘Unfettered’ capitalism. This form of capitalism is distinguished from its trustified or corporatist form. While talking of Intact capitalism, Schumpeter seemed to have had England during the nineteenth century in mind.

⁴⁵ First published in Vienna in 1911/12.

⁴⁶ Schumpeter writes: ‘[T]he capitalist order entrusts the long-run interests of society to the upper strata of the bourgeoisie.’ *Socialism, Capitalism and Democracy*: 160.

Now the question is, whence comes the attack? The question is important because, as we already know, the bourgeoisie has done its duty by working people, and that trade unions generally are not socialist; they are primarily interested in improving the working conditions of their members within the frame of capitalism. So, why the march into socialism? There is no single answer to this question. For instance, Schumpeter (who was writing during the 1940s)⁴⁷ considered the possibility that the establishment of the 'welfare state' may eventually result in a country sleepwalking into socialism. Instead of marching into socialism, we may have socialism by stealth. Another answer, which I think is central to Schumpeter's overall thought is that the threat comes from 'the masses' (though not, as in Marx, from the organised proletariat consciously and rationally attacking the capitalist citadel). It is this line of thinking that we will pursue here.

The problem that is central to Schumpeter's thought is one of social control or social discipline. This is the habit of working people obeying orders and accepting supervision; the habit of accepting the upper strata of society as their social superiors. Now this habit is not the result of any rational calculation on the part of working people. To put it in Schumpeter's own words: 'The workman's readiness to obey orders was never due to a rational conviction of the virtues of capitalist society or to a rational perception of any advantages accruing to him personally.'⁴⁸ Personal and group discipline is inculcated by a disciplining authority. It is inculcated through training and a process of habit-formation. The culture of obedience is then passed on from generation to generation and periodically renewed. The source of this training, the fruits of which the bourgeoisie enjoyed during the period of individualistic capitalism, and even under corporatist capitalism, goes back to the feudal period. It lay in the medieval warlord's ability to lead men on the battlefield. The assumption here is that the quality of leadership on the battlefield extends to social life in general. This ability makes the warlord - a landed aristocrat - a natural leader of men. He possesses 'mystic glamour' that commands obedience. It is this glamour more than anything else that counts in the ruling of men.⁴⁹ The working people transferred part of the respect they showed their feudal lords to their new masters, the bourgeoisie. Life was made easier for the bourgeoisie in this respect because it continued to live, even under individualistic capitalism, in symbiosis with the descendants of the old warlords. The landed aristocracy (as we saw earlier) continued to

⁴⁷The first edition of *Capitalism, Socialism and Democracy*, the book in which Schumpeter's ideas on social evolution are systematically presented, was published in 1942; revised edition was published in 1947; and an enlarged third (and final) edition was published in 1950.

⁴⁸ *Capitalism, Socialism and Democracy*: 214.

⁴⁹ The idea of social discipline used by Schumpeter here is not much different from that of Marx. But Marx attributes the inculcation of social discipline that was present under the capitalism of his day to (among other repressive measures undertaken by the state) the laws against vagabondage and poor laws during the period of primitive accumulation. This issue is extensively discussed in *Capital*, vol. 1, the chapter on primitive accumulation.

manage the machinery of the state, while the bourgeoisie devoted all its energies to economic activity. It therefore continued to enjoy the benefit, in terms of social discipline and of the socio-psychological dispositions favourable to it created during the pre-capitalist period.

However, with continuing economic development the pre-capitalist structure that had provided the bourgeoisie with a protective shield was gradually undermined. (It took some thing like a hundred years, but then, in the context of social evolution this is not a long period.) With economic development eventually undermining the pre-capitalist superstructure, the bourgeoisie lost the protection it had enjoyed and became defenceless against attack.

Now, finally, there are two further questions that need to be answered. First, why can the bourgeoisie (even in its weakened form) not renew the culture of obedience? The answer is quite simple. '[T]he industrialist and the merchant, as far as they are entrepreneurs, also fulfill a function of leadership. But economic leadership of this type does not expand, like the military lord's leadership, into leadership of nations. On the contrary, the ledger and cost calculation absorb and confine.'⁵⁰ The pursuit of profit and that of the Holy Grail are two very different things.

Second, we know, from both Marx and Schumpeter, that capitalist development advances a rational approach to life and create a critical frame of mind. So we are led to ask why the ruling class is unable to argue the case for capitalism on the basis of its utilitarian credentials. Schumpeter's answer is again simple. Political attack cannot be met by reason. Reasoned argument may tear the rational garb of attack but 'it cannot reach the extra-rational driving power that lies behind it'. In any case, 'the masses' are generally incapable of seeing where their true interest lies. They see only monopolistic practices and high profits. To see the case for capitalism they would need to see further than the short run, and that requires powers of analysis that are quite beyond them.

13.

In this paper, I have tried to bring out the similarities and differences between the theories of Marx and Schumpeter. One cannot but agree with Schumpeter that the idea and the aim are the same in the two theories. The 'idea' here refers to the view that social reality is an evolutionary process and that the capitalist economy changes itself by virtue of its own

⁵⁰ *Capitalism, Socialism and Democracy*. 137

inherent logic, and by changing itself it changes the entire social framework.. The 'aim' is to construct a schema that will demonstrate how this transformation may take place. However, the mechanism of change is very different in the two theories. I have argued that the difference is of fundamental importance and that it originates in the very different ways in which Marx and Schumpeter conceptualise the class phenomenon and capitalism.

Schumpeter's admiration for Marx is explained by the latter's 'discovery' of the 'idea' mentioned in the preceding paragraph and Marx's attempt to comprehend all social phenomena within a single theoretical framework. I suggest that it is instructive to make a comparison between Schumpeter's admiration for Walras ('the greatest of all economists'⁵¹ whose work constituted 'the Magna Carta' of exact economics'⁵²) and for Marx. His praise for Walras is based on the view that Walras created an all-embracing theoretical schema in which are determined the equilibrium values of *all* the economic variables so that partial theories dealing with different variables - prices, quantities bought and sold, profits, wages, employment - all become part of an 'all-purpose apparatus of analysis'.⁵³ But Walras' 'Magna Carta' deals exclusively with a stationary economy and it is unable to accommodate within its framework economic and social change that is 'evolving from inherent necessity'. The framework for analysing economic and social change evolving from inherent necessities was 'discovered' by Marx. It is this idea and the fact that Marx attempted to comprehend *all* social phenomena in this framework that inspires Schumpeter's respect and admiration for him. Schumpeter emulates Marx in this respect, creating his own, alternative schema. It is therefore not surprising that he discusses precisely the same issues as does Marx and finds himself in constant dialogue with him, even though his answers are, as Professor Samuelson puts it, '180 degrees from Marx's'.

⁵¹ *History of Economic Analysis*: 827

⁵² *ibid.* 968.

⁵³ *Ibid.* 16.

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