

CAPITALISM, SOCIALISM AND DEMOCRACY 80 YEARS LATER

Looking at capitalism today in light of its past and possible future

A conference from the WEA

1st March to 20th March, 2024

WEA 12 YEARS OF ONLINE CONFERENCES

Institutional change in the post-war period

Daide Gualerzi

1. Introduction

A possibly useful way to think about Schumpeter's book *Capitalism, Socialism and Democracy* today is to look at the two phases of institutional and structural evolution that we have observed in the industrial economies of the West in the post-war period.

Although the analysis does not directly engage with Schumpeter's book, it concerns the crisis of Capitalism – of which he has a distinctive and original, although possibly limited explanation. These two dimensions, structural and institutional, are arguably at the roots of current events.

The paper presents a highly simplified analysis of two relatively well-defined episodes of growth: the "Golden Age", some twenty years after the Second World War, and the last two decades of Neoliberalism.

2. Structural and Institutional analysis

A stylized fact of growth and economic expansion is the process of structural change. In a **survey of structural change** literature (Silva and Teixeira, 2008) the authors note "the analytical difficulties associated with the organization of the relevant literature on structural change analysis." (p.275) It becomes indeed apparent how complex is the definition of structural change.

The survey examines the early foundations of structural change analysis that include Classical authors and Schumpeter. The last section overviews recent trends in structural change analysis and interpretation.

Although widely known and cited Pasinetti contribution (1981, 1993) is listed among the theoretical contributions. This is somewhat misleading

since Pasinetti model, although surely theoretical, lays out some fundamental features of the development of actual economic systems. The most important is that expansion is associated with inherently uneven growth among sectors. That is the question of expanding and declining sectors. Here the similarity with Schumpeter is rather impressive. Although starting from very different premises both Pasinetti and Schumpeter insists on this uneven development of industries as a key factor for the explanation of aggregate investment and aggregate employment, that is, the basics of economic expansion.

Silva and Teixeira (2008) point out that from the point of view of mainstream analysis in Pasinetti model structural change is a "disequilibrium" phenomenon, except it is also the key to the moving system. Precisely as in Schumpeter well-known notion of creative destruction.

We should note that structural change has also being investigated in the perspective of equilibrium analysis. (Laitner, J. 2000. "Structural Change and Economic Growth", *Review of Economic Studies*, Vol. 67, No. 237; Kongsamut, P., Rebelo, S. and Xie, D. 2001. "Beyond Balanced Growth", *Review of Economic Studies*, Vol. 68, No. 237; Ngai, R. and Pissarides, C. 2007. Structural Change in a Multisector Model of Growth, *American Economic Review*, (pp.429-443); Acemoglu, D. and Guerrieri, V. 2008. Capital Deepening and Non-balanced Economic Growth, *Journal of Political Economy*, Vol. 116, no. 3.)

If we remain with the main point made by Pasinetti model of growth and structural change, *i.e.*, the uneven nature of the growth process, it is then clear that such a basic approach to structural analysis needs to be married to a parallel attention paid to the evolving institutional system. It should be recalled also that, especially in recent times, Neo-Schumpeterian-evolutionist scholars, following the analysis of innovation, have engaged with the issue of institutions.

In this brief paper we attempt to ground that analysis in two historical episodes. This direction of research does not even attempt to develop a theory of institutions – that conceivable would require an expertise beyond that of economists. However, examining the role of institutions in specific historical circumstances, some very general lines of evolution can be detected and then subjected to more in-depth analysis.

3. The Golden Age

The 'golden age of capitalism' is associated with Keynesian economic policies in the countries of the capitalist West. (Marglin and Schor, 1992). Successful as it was in generating rapid growth with high employment it was unmade by a combination of events in the 1970s. The monetarist policies and supply-side economics that followed did not succeed in regenerating comparable growth rates.

Interestingly the main focus of the analysis is on the institutional arrangements that went into the making and unmaking of the golden age.

Following the 'regulation' approach (in its original formulation and that of the "structures of accumulation" developed in the US by David Gordon and Michael Piore) mutually reinforcing institutional structures became mutually destructive. This concerns also demand management and the more or less accommodating monetary policy of central banks. The capacity of a country to maintain high levels of employment it is argued depended crucially on the appropriate social, economic, and political institutions, along with the ability to mobilize effective coalitions to act through these institutions. Essential aspects such as the relationship between real wages and investment, and hence employment, are associated to different economic regimes.

The golden age was especially in the Far East. The Japanese success story (much in vogue in the 1980s) was centered on Japan being at the forefront of the OECD countries for the rate of growth of labour productivity. Thus, the contrast between the organization of production in Japanese and Western firms.

4. Neoliberalism

We venture now into the analysis of the second period, focusing on the latest twenty years of "Neoliberalism". We nevertheless want to draw at least a sketch of this growth episodes because it that highlights an interesting parallel with the Golden age with reference to the rise and collapse of the institutional setting.

To clear the ground from the surely difficult problem of defining Neoliberalism we will simply refer to a phase started with the Thatcher and Reagan "revolutions" in the 1980s in the UK and the US. For the economic foundations of Neoliberalism, it will suffice for our purposes Stiglitz interpretation (2002): The triumph in economic theory and policy of pre-Keynesian ideas.

Most important is for our purposes is what Palley (2012) says about Neoliberalism. He argues that the 2008 financial crisis incubated a long-term stagnation. Both are the result of the "faulty US macroeconomic

paradigm that has its roots in Neoliberalism which has been the dominant intellectual paradigm.” (p.4) The fundamental aspect is “the dismissal of the classic Keynesian virtuous circle of growth...the abandonment of the commitment to full employment, an exclusive focus of controlling inflation (well beyond the employment- inflation trade off), thus severing the productivity wage link. In other words, the key institutional turn occurring with Neoliberalism is precisely the overturn of the institutional framework that was so prominent in the success story of the Golden Age. The result of the dismissal of what we can all the Keynesian compromise are fully displayed after about thirty years.

Following Palley’s argument we can conclude that crucial changes concern the institutions of corporate globalization, where we can also locate the rise of modern finance, the institutions regulating the labour market, with a shift to flexible labour markets That includes the persistent pressure on unions aimed at the dismantling of their bargaining power.

Why did the US capitalism embrace the neoliberal course? According to Palley was the result of “true intellectual belief, self-serving ideology, or a combination of both.”

5. Institutions and structural change

The two institutional frameworks briefly examined above are actually one the mirror image of the other. The Keynesian distributive compromise after World War II, sustained by rapid productivity growth, was progressively taken over by a pre-Keynesian set of ideas and policies.

In both cases the macro performance is associated to a specific set of institutions. Interestingly, very little attention, if any, is paid to the “structure” of the economy, its changes, and its role in determining macro performance. However, an important process of structural transformation characterizes both periods. In the first case the focus is on the rise of mass production and modern manufacturing. Neoliberalism can instead be associated especially in the last two decades to the structural transformation driven by the development of ICTs.

At this stage of the research, we would like to pose two questions for further investigation and discussion.

1 - It can be noted that there is no explicit discussion of structural change and its implications for productivity growth during the Golden Age. Nor the tarnishing of the institutional framework (the structures of accumulation) is much connected to changes in the economic structure. How do we explain then the rise and the decline of institutions?

2 - Whereas it is clear, at least in general terms, the role played by the institutions of the Keynesian compromise in the economic success of the Golden Age, it remains much more complicated to explain why the structural transformation rooted in the ICTs-driven industrial restructuring

is combined – or even needed – the drastic institutional change of Neoliberalism. In other words, why did the structural transformation imply the end of the Keynesian compromise?

Concluding remarks

The focus of the paper is primarily:

- a) on the institutional arrangement that appear to be so much part of the success story of the Golden Age;
- b) on the structural change driven by the quite distinct technological bases and industrial dynamics of the two periods.

We are clearly referring to institutional analysis in a broad sense, much larger than the notion of “the rules of the game”. The reasoning follows very general lines that require more investigation to draw further implications for the crisis and the prospects of Democracy and Socialism.