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Capitalism

Capitalism: one kind of economy

This book focuses mostly on describing one very particular kind of economy: capitalism.

There, I've said it: the "C-word." Just mentioning that term sounds almost subversive, these days. Even talking about capitalism makes it sound like you're a dangerous radical of some kind. But we live in a capitalist economy, and we might as well name it. More importantly, we might as well understand what we are dealing with.

Curiously, even though capitalism dominates the world economy, the term "capitalism" is not commonly used. Even more curiously, this word is almost *never* used by economists. Neoclassical economics is dedicated to the study of capitalism; in fact, other kinds of economies (that existed in the past, or that may exist in the future) are not even contemplated. Yet the term "capitalism" does not appear in neoclassical economics textbooks.

Instead, economists refer simply to "the economy" – as if there is only one kind of economy, and hence no need to name or define it. This is wrong. As we have already seen, "the economy" is simply where people work to produce the things we need and want. There are different ways to organize that work. Capitalism is just one of them.

Human beings have existed on this planet for approximately 200,000 years. They had an economy all of this time. Humans have always had to work to meet the material needs of their survival (food, clothing, and shelter) – not to mention, when possible, to enjoy the "finer things" in life. Capitalism, in contrast, has existed for fewer than 300 years. If the entire history of *Homo sapiens* was a 24-hour day, then capitalism has existed for two minutes.

What we call "the economy" went through many different stages en route to capitalism. (We'll study more of this economic history in Chapter 3.) Even today, different kinds of economies exist. Some entire countries are non-capitalist. And within capitalist economies, there are important non-capitalist parts (although most capitalist economies are becoming *more* capitalist as time goes by).

I think it's a pretty safe bet that human beings will eventually find other, better ways to organize work in the future – maybe sooner, maybe later. It's almost inconceivable that the major features of what we call "capitalism" will exist for the rest of human history (unless, of course, we drive ourselves to extinction in the near future through war, pollution, or other self-inflicted injuries).

So we shouldn't understand "the economy" and "capitalism" as identical. They are two different things. In this book we will study capitalism, as the dominant current form of economic organization. But we must always distinguish between what is *general* to all types of economy, and what is *specific* to capitalism.

What is capitalism?

There are two key features that make an economy capitalist.

1. Most production of goods and services is undertaken by privately-owned companies, which produce and sell their output in hopes of making a profit. This is called PRODUCTION FOR PROFIT.
2. Most work in the economy is performed by people who do not own their company or their output, but are hired by someone else to work in return for a money wage or salary. This is called WAGE LABOUR.

An economy in which private, profit-seeking companies undertake most production, and in which wage-earning employees do most of the work, is a capitalist economy. We will see that these twin features (profit-driven production and wage labour) create particular patterns and relationships, which in turn shape the overall functioning of capitalism as a system.

Any economy driven by these two features – production for profit and wage labour – tends to replicate the following trends and patterns, over and over again:

- Fierce *competition* between private companies over markets and profit.

- *Innovation*, as companies constantly experiment with new technologies, new products, and new forms of organization – in order to succeed in that competition.
- An inherent tendency to *growth,* resulting from the desire of each individual company to make more profit.
- Deep *inequality* between those who own successful companies, and the rest of society who do not own companies.
- A general *conflict* of interest between those who work for wages, and the employers who hire them.
- Economic *cycles* or "rollercoasters," with periods of strong growth followed by periods of stagnation or depression; sometimes these cycles even produce dramatic economic and social crises.

Some of these patterns and outcomes are positive, and help to explain why capitalism has been so successful. But some of these patterns and outcomes are negative, and explain why capitalism tends to be economically (and sometimes politically) unstable. The rest of this book will explain why these patterns develop under capitalism, and what (if anything) can be done to make the economy work better.

Capitalism began in Europe in the mid-1700s. Until then, these twin features – production for profit and wage labour – were rare. In pre-capitalist societies, most people worked for themselves, one way or another. Where people worked for someone else, that relationship was based on something other than monetary payment (like a sense of obligation, or the power of brute force). And most production occurred to meet some direct need or desire (for an individual, a community, or a government), not to generate a money profit.

Capitalism and markets

Even when economists bother to "name" the economy they are studying, they usually use a euphemism instead of the "C-word." They don't call it capitalism. They call it a "market economy." This implies that what is unique about capitalism is its reliance on markets and market signals (like supply, demand, and prices) to organize the economy. But that is wrong, too.

Markets of various kinds do indeed play a major role in capitalism. A market is simply a "place" where various buyers and sellers meet to haggle over price and agree on sales of a good, a service, or an asset. (By "place," I do not mean that a market has to have an actual physical location – it just needs to provide a way in which buyers and sellers can communicate and strike deals. In the internet era, markets can exist in cyberspace, not just at a community hall or stock exchange.)

Markets usually (but not always) imply some kind of competition, in which different buyers and sellers compete with each other to get the best deal. We will study the particular nature of competition under capitalism in detail in Chapter 11.

But capitalism is not the only economic system which relies on markets. Pre-capitalist economies also had markets – where producers could sell excess supplies of agricultural goods or handicrafts, and where exotic commodities (like spices or fabrics) from far-off lands could be purchased. Most forms of socialism also rely heavily on markets to distribute end products and even, in some cases, to organize investment and production. So markets are not unique to capitalism, and there is nothing inherently capitalist about a market.

Just as important, there are many aspects of modern capitalism that have nothing to do with markets. Within large companies, for example, very few decisions are made through market mechanisms. Instead, relationships of command, control, and plan reign supreme. (Remember, some corporations are economically larger than many countries, so these internal non-market relationships are important.) And there are other ways in which capitalism reflects powerful *non-market* forces and motivations – like tradition, habit, politeness, reciprocity, altruism, coercion, even (sometimes) brute force.

By pretending that capitalism is a system of "markets," economists imply that it is based on relationships between essentially equal parties. Neoclassical economists study two main kinds of markets: markets for FACTORS OF PRODUCTION (things that are used in production, like labour, land, and natural resources), and markets for the final GOODS and SERVICES produced with those factors. Neoclassical economists even describe the relationship between a large company and its workers as a form of market exchange. Everyone comes to the "market" with something to sell, and in theory they're all better off (than they were in the first place) as a result of trading in that marketplace.

Imagine a bustling bazaar, to represent the whole economy. In one corner of the hall is General Electric, which brings US$500 billion worth of capital assets to the market. In the other corner are some workers, with only their brains and brawn – their intelligence and their physical strength – to sell. Will a trade between these two sides be equal or voluntary, in any meaningful sense of those words? Not at all. And neoclassical economics doesn't bother explaining the historical process by which one stall at the bazaar is stocked with US$500 billion in capital, while another is stocked with just hard-working human bodies.

By pretending that capitalism is just a system of "markets," neoclassical economics deliberately blurs the real power relationships, and the often-violent historical processes, which explain the economic system we actually live in. Yes, we must study markets when we study capitalism – their flaws, as well as their virtues. But markets are not the idealized institutions portrayed in economics textbooks. And capitalism is equally shaped by other, non-market forces and structures, too.

So capitalism is not a "market economy." Capitalism is a system in which most production occurs for private profit, and most work is performed by wage labour.

Fads in capitalism

Of course, capitalism can change its "look" a lot, while still preserving its core, underlying features. Many economists and commentators have argued that capitalism today is not at all like capitalism in its early days (back in the soot and grime of the Industrial Revolution). These are some of the ways in which modern capitalism is supposedly a "new" system:

1. **The "post-industrial" economy** As discussed in Chapter 1, every economy produces both goods and services. Over time, a growing share of total value added in advanced capitalist countries consists of services. Today, services account for about 70 percent of GDP in advanced economies – and an even larger share, if we count non-traded output, like housework. The shrinking importance of goods is partly because technology and globalization have reduced their costs compared to services, and partly because most consumers prefer to buy a greater proportion of services (especially "luxuries"

such as restaurant meals and tourism) as their incomes rise. As large-scale industry becomes less important in the big economic picture, some economists argue that capitalism has changed, and that old stereotypes about "workers and bosses" no longer apply in this post-industrial system.

2. **The "information" economy** A related argument suggests that the advent of computer technology and the internet have created a fundamentally new economy – one centred on information, rather than commodities. Some pundits simply called this the "new economy." They even argued it would be immune to the traditional boom-and-bust cycles of earlier times. This theory was popular in the late 1990s, and helped to justify the ridiculous behaviour of internet-mad stock markets during this time. Beginning in 2000, however, the "dot-com" stock market boom collapsed (like all other stock market bubbles before it), and investors lost trillions of dollars. Since then, jargon about the "information economy" has become much less popular.
3. **The "shareholder" economy** Some observers have focused on the role played by pension funds, mutual funds, and other so-called "institutional" investors in modern stock markets. They argue that capitalism is fairer than it used to be, since more individuals now own shares and other forms of financial wealth (either directly, or indirectly through mutual and pension funds). They claim that this new "shareholder" system has somehow "solved" the age-old conflict between workers and capitalists.

There is a grain of truth in each of these portrayals – but only a grain. And in no case is it reasonable to conclude that capitalism has *fundamentally* changed.

Yes, services are increasingly important. But many services are produced in large-scale, factory-like workplaces. Think of a long-distance call centre, with hundreds of workers sitting in small cubicles, whose work is electronically paced and constantly monitored. And the services sector of the economy is still dominated (just like goods-producing industries) by profit-seeking private companies, many of them very large – and very profitable.

Yes, information is more important and faster-flowing than ever. But people cannot "eat" information; it is economically useful mostly as an input to other, more traditional goods and services industries.

And far from ushering in a new era of decentralization and supposed "participation," computer-related industries are still dominated by huge, profit-hungry companies (like Microsoft and Google).

Yes, pension and mutual funds are important players in stock markets. But the vast majority of financial wealth is still owned the old-fashioned way: by a surprisingly small elite of very wealthy families. In fact, in most capitalist countries financial wealth has become *more* concentrated among the rich, not less (we will discuss this in more detail in Chapter 7).

So while capitalism produces more services and less goods than it used to; while companies rely on sophisticated computer technology to manage their affairs; and while a significant proportion of households in the developed countries own *some* financial wealth (but not much, in the grand scheme of things), the core features of capitalism are still very much visible. Most production is undertaken by profit-seeking private companies. And most work is performed by people who do not own those companies, but who instead must work for wages. There is still incredible inequality, and an inherent conflict of interest, between the people who own successful companies, and the rest of us.

In short, there's nothing much "new" about capitalism at all.