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A Critique of Political Economy

II. A Post-Mortem on Cambridge Economics*

By FRANZ OPPENHEIMER

Was wankt, soll man auch noch stossen.†

FRIEDERICH NIETZSCHE

Introduction

NEARLY HALF A CENTURY ago the present writer laid the first foundations of his theory of economics, now completed. Since that time he has seen four schools of economic thought, which then were competing for predominance, pass into the discard.

The classic, or rather the post-classic "bourgeois" school of economics was already doomed beyond hope when John Stuart Mill felt himself honor bound to abandon the wage-fund theory and, with it, the complete theory of distribution. The "Historical School of Economics" was the first of its assailants to vanish almost without leaving a trace, breaking down under the onslaught of scientific Marxism on the one hand, and the different schools of marginal utility on the other hand. Both of the conquerors, a generation later, had lost almost the last of their devotees.

"Bourgeois" economics—the theory that attempts to justify existing property relationships—attempted in vain to win new strength by adopting parts of its adversaries' ideas, first of socialism, then of marginalism. The result, in the former case, was "the socialism of the chair," which expired with its great representative, Adolph Wagner. The second attempt was that of the Cambridge School of Alfred Marshall and his pupils. It had no better fate; it is bankrupt as well, as is acknowledged by its best men, such as, for example, John Maynard Keynes:

Modern theories on economics are mere concoctions as imprecise as the initial assumptions they rest upon, which allow the author to lose sight of the complexities and interdependencies of the real world in a maze of pretentious and unhelpful symbols.¹

The same is very moderately expressed by Maurice Dodds:

The social philosophy underlying it represents, like that of John Stuart Mill, nineteenth century bourgeois liberalism with a bias toward social re-

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† *What is staggering ought to be pushed.* From Zarathustra.

¹ "The General Theory of Employment, Interest and Money," German tr., p. 252.

form. . . . In recent years doubt has increased rather than diminished. The post-war generation is more sceptical than its sire and is more conscious of the loose ends that still remain untied; it recognizes that, particularly in the theory of distribution, there is still much that is confused and uncharted, perhaps internally inconsistent.²

This essay will seek to discover the cause of these judgments within the theoretical structure of the Cambridge School, by an analysis of its fundamental work, Marshall's "Principles of Economics."³

I

Definition of Economics

THE FIRST ERROR of moment in Marshall's system is the misunderstanding of what economics is. Marshall defines it as

a study of mankind in the ordinary business of life; it examines that part of individual and social action which is most closely connected with the attainment and with the use of the material requisites of well-being. Thus it is on the one side a study of wealth; and on the other, and more important side, a study of man.⁴

And again:

Economics is thus taken to mean a study of the economic aspects and conditions of man's political, social and private life; but more especially of his social life.

This definition is utterly incorrect. It assigns to economics a great many of the problems that belong to general sociology. This is realized when one considers the remainder of the first, introductory chapter. It tells how "the character of man has been moulded by his everyday work and his religious ideals," how poverty is apt to spoil the character and the race. It asks whether "we may not outgrow the belief that poverty is necessary." It assures us that "the fundamental characteristic of modern industrial life is not competition, but self-reliance, independence, choice and forethought," that "man is not more selfish, nor more dishonest than he was," and that "dreams of a Golden Age are beautiful but misleading," etc.

The consequence of this erroneous foundation is that the book is not in the least what its title indicates, an exposition of "principles," i.e., a *system* of logically-connected tenets covering an exactly limited field of facts and presenting in their totality the doctrine of *theoretical* economics, neither

² Maurice Dodds, "Economics," *Encyclopaedia of the Social Sciences*.

³ Eighth edition, New York, 1925, hereafter cited as "P.E."

⁴ P.E., I, I, 1.

more nor less. It is a work that brings together a wealth of facts and opinions on all three branches of *practical* economy (private economics, public finance, and economic policy, particularly industrial, but also agricultural economic policy). Here and there, there is, moreover, the *disjecta membra* of almost all the social sciences: individual and social psychology, general sociology, history, theory of statistics, moral science: a catch-all of facts and intimate and tentative opinions "*de omnibus rebus et aliquot aliis.*" Some minor problems are expatiated upon, some major ones ignored or dodged. It reminds the expert of Gustav Schmoller's *Volkswirtschaftslehre*, which, precisely in the same manner, attempted to mire economics in a hotchpotch of social science—or what he believed to be science. The attempt miscarried there as here; it is bound to miscarry whenever it is made. Marshall himself realized it:

Economics has made greater advances than any other branch of the social sciences, because it is more definite and exact than any other. But every widening of its scope involves some loss of this precision.⁵

He is forced to confess that "the science is still in its infancy"⁶ and that "it can never become a simple science."⁷

The same imperialistic tendency of expanding the scope of economics was at the root of the Institutional School. Wesley C. Mitchell disclosed this in his remark:

The future of economics, the question whether man will ever succeed in establishing a serviceable science of human behaviour, becomes one of the crucial issues on which hangs the doubtful fate of mankind.⁸

But human behaviour is the problem, not of economics alone, but of general sociology and the special sociologies, especially of social psychology. Economics is concerned neither with the motives nor with the aims of human behavior, but merely with the means that are usually employed to attain desired goals. This is clear by the following definition:

Economics is the science of the social economy of the economic society (or of the group economy of the economic collectivity). It is, as the definition indicates, one of the social sciences. It shares with them the common "subject of experience," the "historico-societarian reality" (Dilthey), and, like all the others, it prepares its own "subject of cognition" by select-

⁵ P.E., Appendix E, 6.

⁶ P.E., I, I, 30.

⁷ P.E., V, VIII, 1.

⁸ Quoted by E. L. Bogart, "Economics," *Encyclopaedia Americana*.

ing out of this enormous mass the phenomena that have particular interest for it: economic actions and their creations in space and time. In other words, its data are concerned with the *process* through which a group secures and takes care of the things of value that its members desire and are able to obtain.

Economic actions are distinguished from all other kinds of action by the following characteristics:

1. They are motivated by the desire of having something (or of having the power of disposal over something), but not by the desire of doing something.
2. They are neither instinctive nor impulsive, but considered, and especially rational actions, i.e., actions conforming to the principle of the minimum means.
3. The things desired are things of value; this means they are not free goods, but are "scarce," costing expenditure either of labor or of possessions of other things of value.

II

Conflict of Economic Motives

THIS CONFUSION REGARDING the scope and the task of economics rests entirely on the erroneous assumption that the science is concerned with the conflict of the motives of economic action:

The measurement of motive thus obtained is not indeed perfectly accurate; for, if it were, economics would rank with the most advanced physical science, and not, as it actually does, with the least advanced.⁹

Marshall has a very adequate knowledge of this conflict or this "crossing of motives" and of the decisions to which it leads:

First, decisions as to the relative urgency of various ends; secondly decisions as to the relative advantages of various means of attaining each end; thirdly decisions based on these two sets of decisions as to the margin up to which the person could most profitably carry the application of each means to each end.¹⁰

This is perfectly true. The decisions as to the first and second point make the action considered, and the decision as to the third point makes it rational. It is incorrect, however, to say that this process of considering and choosing is a subject matter of economics. Economics, as Marshall himself defines it is "a study of individual and social *action*," but not of the process preceding it which belongs exclusively to psychology proper.

⁹ P.E., I, II, 7.

¹⁰ P.E., V, IV, 4.

Economic action does not *begin* before the moment when the decisions are made, first, which of the conflicting desires is to be satisfied; secondly, which thing of value, apt to satisfy this preferred desire, is to be secured; and, thirdly, to what extent it is to be secured. And, on the other hand, economic action does not *last* beyond the moment when the coveted thing of value is attained. Between these two points, decision and goal, there is not the least obstacle; economic action has run its course, unhampered by the conquered motives and desires.

Economic science, therefore, is concerned neither with the motives which precede, nor with the applications of the secured things of value to either consumptive or technical purposes which follow the action of securing them. And, for this reason, in spite of what Marshall opines, it is a simple science, and even capable, in spite of what Cairnes opined,¹¹ of arriving at quantitative formulas.

III

The Equilibrium

IT HAS BEEN SAID that the group economy of the economic collectivity is a process. It is one of those processes activated by antagonistic forces which can be explained satisfactorily only by determining the equilibrium toward which these forces, in our case supply and demand on the market, are tending.

Such an equilibrium is called "static" in physics. Auguste Comte, who was an outstanding physicist, introduced the term into sociology; and his disciple, John Stuart Mill, into economics. Then John Bates Clark, especially, stressed the necessity of determining economic statics as the only possibility of attaining the highest goal of this as of all sciences: to arrive at quantitative formulas. It is, however, true, as Joseph Schumpeter emphasizes, that all good theory from its first beginnings in physiocratic doctrine was "essentially static," without being conscious of it; it is, as the great mathematician Cournot put it, a necessary assumption.

Adam Smith, almost two centuries ago, solved the crucial problem of determining accurately economic statics, but failed to realize that his formula is the very pass-key to all closed doors in economics.

The whole of the advantages and disadvantages of the different employments of labour and stock must, in the same neighborhood, be either perfectly equal or continually tending to equality.¹²

¹¹ "It is hopeless that we should have ere long an exposition of economic principles drawn up in quantitative formulas." J. E. Cairnes, "Some Leading Principles of Political Economy."

¹² "The Wealth of Nations," Bk. I, ch. 10.

Almost a century later Johann Heinrich von Thuenen wrote:

The equilibrium takes place when, through the price of the commodities, labor of equal quality is equally rewarded in all branches of production; and this average reward is the measuring rod for the costs of production and for gain and loss.¹³

The equilibrium, therefore, is that level of prices where all producers enjoy the same income from the gains on the prices of their products, unless differences of qualification and, as Smith added, monopolies, cause divergences.

This can be expressed in a very simple quantitative formula. Let us call Thuenen's "average income" (i.e., the amount of money which is the income of the greatest group of equally-qualified producers) J , and denote by $\pm q$ the higher or lower earnings of more or less qualified producers; and by $\pm m$ the gain of a monopolist or the loss of a monopolist's victim. Then the equilibrium is attained when the income of any member of this society (J_1) is determined by the formula:

$$J_1 = J \pm q_1 \pm m_1$$

The present writer has shown elsewhere that this formula is the starting point from which the quantitative formulas for static value and for wages, profits and rent easily can be deduced.

This clear and simple determination of statics has been ignored and forgotten by "bourgeois" economists, as almost all other achievements of theory have been ignored and forgotten. Marshall is no exception. Like his predecessors, he was under the delusion that he had solved the problem by resorting to the interplay of supply and demand:

The normal price being thus determined at the position of stable equilibrium of normal demand and normal supply.¹⁴

This eighth edition of the "Principles" was published in 1925; but Thuenen, one of the most venerated of Marshall's authorities, had written as long before as 1850 that

this explanation, confounding the conceptions, takes the facts for the explanation of the facts, the manifestation for what causes the manifestation.¹⁵

And Boehm-Bawerk wrote that it "gives husks instead of grain." Marshall obviously believed he had evaded this trap because he determines supply and demand with the refined methods of Gossen's marginalism, but it remains

¹³ "Der isolierte Staat," (1826-63), Ed. Waentig, 1921, p. 529.

¹⁴ P.E., V, III, 1.

¹⁵ *Op. cit.*, p. 436.

the old merry-go-round of thought: the normal price obtains at the position of stable demand and supply; and this position obtains when prices are normal. It is the prettiest sample imaginable of a vicious circle.

Under these circumstances Marshall is compelled to confess:

The pure theory (of equilibrium) in its earlier stages diverges but little from actual facts; but, if pushed far, its practical value rapidly diminishes.¹⁶

IV

Comparative Statics

IN ORDER TO COMPREHEND fully what is to be achieved and to what extent efforts have failed, some words must be said on the method of statics to be employed in economics. The present author was the first to distinguish between the methods of simple statics and of comparative statics. The former is to be employed in simple processes, i.e., processes where there is no development, or where we are not interested in an existing development. It consists in determining the equilibrium and measuring the "kinetic" deviations caused by "disturbances" from without the system. Thus, for example, the height of the tides is measured by referring to the static "zero-level" of the ocean.

Where there is a process of development in which we are interested, this simple method must be supplemented by comparative statics, comparing different successive static levels. To illustrate by an example: a physician examining a sick person employs the method of simple statics when he judges the significance of his temperature, etc., by the data of statics, i.e., health. But, when examining a healthy child, he employs the method of comparative statics by referring weight, height, intelligence, etc., to the data normal to a child of that age and sex, to find out whether the particular child under examination shows normal or abnormal development.

The social and especially the economic process is a process of evolution which must be correspondingly treated.

Kinetics has for its objective competition. It shows how, in the concatenation in space and time of the markets, prices continually approach to that level, described by Adam Smith and Thuenen, where each producer earns the income falling to him according to his qualification and his position as to monopolies.

Statics has for its main objective distribution. It studies to what extent differences of qualification and monopolies are responsible for the divergences from the "average reward of labor" in our "capitalist" society; or

¹⁶ P.E., V, XII, 3.

why the social product is divided at all, and why in precisely these, "given" proportions into wages, profits and rent.

Comparative statics has for its objective the "tendency of evolution," studying signally the effect of increasing population and its sequels in higher graduated co-operation, improved technique and growing output per capita in industry and agriculture.

The only thing that can possibly be said to recommend the manner in which Marshall has treated this essential subject matter of statics is that he possessed a faint notion of comparative statics. He discriminates between what is "normal" in short and long periods.¹⁷ He is, however, much too much concerned with the fluctuating market prices which are of the highest interest for his "businessman," but of only slight interest for economic theory, to understand fully the importance of this discrimination. He writes, for example:

Normal costs of production and reproduction are controvertible terms.¹⁸

This, however, is true merely as a simple static consideration, because here supply and demand, it is assumed, remain unchanged. But it is decidedly wrong for comparative statics, when account is taken of the laws of increasing and diminishing returns. He himself writes:

The statical theory of equilibrium is therefore not wholly applicable to commodities which obey the law of increasing returns.¹⁹

This is only one, and certainly not the worst, example of the indeterminateness and indistinctness prevailing in these chapters; it is the same confusion of which we had cause to complain in the first section, of elements which it was our task to disentangle and cleanly to separate.

¹⁷ P.E., V, V, 1.

¹⁸ P.E., V, VII, 5.

¹⁹ P.E., V, XV, 4.

(Continued)