

Economics and the 'Manchester system' (editorial)

Urban Sušnik

Exactly a hundred years ago, in his *magnum opus*, *The General Theory of Employment, Interest and Money*, Keynes saw capitalism as a system with many faults, yet he nevertheless believed in its redeeming qualities and he therefore set out to try and keep intact the system of private initiative, whilst augmenting it with a more active role of the state, which would alleviate some of the grievances that a large part of the populace had with the status quo. Keynes (2003) finds two main faults of what he also calls the 'Manchester system': the first is its inability to provide full employment, the second is its arbitrary and inequitable distribution of wealth and income. Fast forward just shy of a century and we see a prominent French economist, Thomas Piketty, writing a bestselling book where, using different methods, his conclusions are very of Keynes: capitalism is a wonderful system and all that it requires in its current iteration is some minor tweaks. While the two authors use completely different approaches to get to their conclusions, their social philosophy is nevertheless very similar. Their aim is essentially to harvest the productive capacity of capitalism, while somehow trying to distribute the spoils that it produces, bringing about what come call capitalism with a human face or what I have called the enlightened capitalism (Sušnik, 2016, p. 160). The main tenet of this social philosophy is a general belief that capitalism as a system of production can somehow be tamed to produce, more or less, only the desired results.

I think this view, while certainly noble, is ultimately flawed and rests on a mechanistic view of capitalism. In 1943 Kalecki disputed Keynes' view of being able to maintain full employment policies for protracted periods of time, because the business and the rentier classes would be against this sort of an arrangement. Kalecki understood that for the Manchester system to operate - in order for the system of production to work as it had - what was required was a constant reminder to the worker that she or he can get fired. But this is only a credible threat if by being fired the worker's livelihood is

somehow threatened, which cannot be the case in a system of full employment. In other words, what happens is that the system of discipline in *production* breaks apart. Kalecki (1943) notes, that this does not have to be so, and that full employment can be attained in capitalism, if there is some other social pressure put upon the workers to accept the general rules in the capitalist mode of production and he points to fascism being able to provide this, by employing political measures that produce a similar sort of coercion for the working class. However, without this exogenous coercive stimulus, capitalism cannot function with permanent full employment and while the reasons often listed by mainstream economists have mainly to do with inflationary pressures, those pressures are not the cause of the problem, they are the consequence of a breakdown in the normal working of the system, which is built on a principle of scarce employment opportunities to maintain social discipline.

While a lot of snarky remarks have been directed at Adam Smith and the now infamous and often misinterpreted concept of the 'invisible hand', there is something to be said for capitalism being essentially a spontaneous system with certain immanent tendencies. And therein lies the problem for Keynes and Piketty. According to their mechanistic vision of capitalism, we can keep its incredible productivity, whilst at the same time getting rid of its inequities, yet what they fail to see is that those very same inequities are what ensures its productivity as well. There is indeed an invisible hand that regulates the workings of the Manchester system, but it is not just the benign hand of Adam Smith in the sphere of exchange, it is also the grotesque paw of Karl Marx and his reserve army of labour in the sphere of production. The normal workings of capitalism require a constant presence of unemployment because this is how the system maintains social discipline in the sphere of commodity production. It is therefore complete correct to view capitalism as a spontaneous order, much in the same way as Hayek, Smith and Marx saw it. And one can also see why the system is efficient in comparison to previous societal arrangements, because in the feudal mode of production or within a slave holding society, you actually needed to employ a group of people to force another group of people to work.

This was not only inefficient because one group of people did not do socially productive work, but because even the group of people that did do productive work (serfs, slaves), was not as motivated as workers under capitalism. Because if you don't work hard in comparison to your peers in capitalism, you will get fired. Stockhammer

and Ramskogler (2008) make an interesting observation on this point as well, saying that in other modes of production your fate was sealed and certain, whereas the mechanism that keeps workers on their toes in capitalism is uncertainty regarding the state of future employment. A worker's future and his incentives are much more aligned with their employer than in any previous mode of production, if a company succeeds you keep your job, if it does not, you are out of work, whereas if a new feudal lord took over some land, the serfs did not lose their livelihood – their life was usually much the same as it had been under previous management.

If the state were to wish and alleviate unemployment in some sort of Keynesian fashion, this will not be welcomed by the capitalist class, because then the very nature of this spontaneous order in which they themselves are the upper echelon of society, becomes threatened. This is why, through most of its history, the capitalist state has in fact been in favour of policies which helped fuel capitalist production, very consciously promoting, either at home or abroad, the conditions that fostered the 'spontaneous' operation of capitalism. Karl Polanyi claimed that *laissez-faire* capitalism was in fact a planned system and that it was the centrally planned economies which were actually a historical fluke. This does not mean, however, that once instituted, even though in a very conscious intervenistic fashion, the Manchester system does not conform to some inescapable tendencies. It also means that certain requirements, such as the existence of a reserve army of the unemployed, have to be met in order for the system to operate smoothly, without any conscious outside intervention.

Of course, the normal workings of the system are not only characterised by its maintenance of social discipline by producing uncertainty with regards to future income flows and thus the livelihood for the majority of the population. As Shaikh (2016, p.14) puts it, competition pits seller against seller, seller against buyer, buyer against buyer, capital against capital, capital against labour and labour against labour. It is a war of everybody against everybody, *bellum omnium contra omnes*. And while capitalism has lots of critics, there is a sort of grotesque beauty in how it can regulate itself, simply by the manifestation of its own inner tendencies. Businesses are in the business of actively cutting costs, because that not only makes them more profitable at existing prices, but it allows them a safety buffer in the future – actively minimising costs is an insurance policy in an uncertain world. This process by itself makes sure that there is always a steady stream of new unemployed. However, it would be wrong

Editor's corner

to assume that this is always the case and in an economic upswing, it can very well be the case, that as firms compete, this stream of technologically redundant workers will be dwarfed by new hiring, due to a general increase in demand. As this shift occurs unemployment decreases and eventually labour starts to ask for higher money wages, if it seems likely that the high levels of employment are going to be maintained for the foreseeable future. This can effectively have one of two results: either firms increase prices along with the wage increase, leading to inflation, or prices stay the same, leading to an increase in real wages and a decline in real profits. Note that without any state intervention, or any other *conscious* outside intervention, this state of things cannot but decay as quickly as it came to be, for once profits decline, firms start thinking of new ways to cut costs, some firms will not be able to repay their financial obligations, which means they will go under, their capitals destroyed and their workers losing their jobs, all of which will by itself create new unemployment and bring down wage demands by the workers.

Traditional economics tries to capture the essence of social reality through the lenses of methodological individualism, looking at the world through the eyes of an individual maximising her or his utility. Yet within the spontaneous order of capitalist production, there are very few things that are left to the individual, because the underlying logic of the system limits the amount of options that one can choose from. To maintain competitiveness over the long run, firms are forced to preemptively cut costs, workers are forced to look for jobs irrespective of their preferences and financial capital is forced to move from one industry to another, or from one country to another in search of higher returns, irrespective of the chaos it leaves in its wake. These, and many others are simply the unintended quintessential emergent properties and logical outcomes of production being organised as a constant jockeying for greater profits (Shaikh, 2016, p. 14). Building your analysis from the ground up, starting with the individual, does not make sense in a complex system, which largely determines the actions of the individuals in the first place. By doing that you are essentially employing an ideological exercise by trying to prove, that the system somehow exists because of these individual actions and is therefore a reflection of the individual, with her or his wants essentially determining social reality.

This is a very archaic way of thinking about complex systems. Additionally, there is a huge discrepancy between the actual world and canonical neoclassical models. Of

course, these discrepancies can be explained with various imperfections, much in the same way that the geocentric view of the solar system could explain how the solar system moves about, if additional assumptions were added into the fold. These same movements could be explained by a simple shift to the heliocentric model, with no need for any additional assumptions. When we talk about complex social systems, and forgetting the ideological implications of methodological individualism, the main reason why you need to study them differently are basically analytical. Taleb (2016) gives a good explanation of this:

'The main idea behind complex systems is that the ensemble behaves in way not predicted by the components. The interactions matter more than the nature of the units. Studying individual ants will never (one can safely say never for most such situations), never give us an idea on how the ant colony operates. For that, one needs to understand an ant colony as an ant colony, no less, no more, not a collection of ants. This is called an "emergent" property of the whole, by which parts and whole differ because what matters is the interactions between such parts.'

Going back one hundred years, Keynes had already begun to grasp that complex social systems, require a different analytical toolset to the one that had been provided at the time by traditional economic theory. To be sure, Keynes was not quite able to rid himself of the old modes of thought, yet by the time he had written *The General Theory*, he had already understood that actions of the individual do not always translate into the aggregate. In other words, there is a discrepancy between the maximising agent and the actual results that come about. A chasm opens between the intentions of the individual and the aggregate consequences, something that is impossible within bounds of traditional theory, where there is no difference if the economy is made up of one person or of a million people, for each person is a complete microcosm of society.

Yet once we allow for this gap in the intentions and the actual consequences, one has to question the validity and usefulness of methodological individualism in trying to understand a complex system like capitalism. In fact, not only is methodological individualism not helpful in understanding capitalism, it might in fact obscure our study of it. Or as Patnaik (2009, p. 71) explains:

'A mysterious element interposes itself between the intentions in their totality and the outcome in its totality. In such a situation, it is this element that demands center stage in analysis: the analysis of individual motivations and actions then becomes altogether secondary. Methodological individualism

then, in a strict sense, that is, unless used merely to flesh out an analysis centering on this mysterious element (in which case we would hardly be justified in calling it methodological individualism at all), becomes a real obstacle to understanding.'

There are various reasons why methodological individualism became so prominent in economics, but one of those reasons is the attempt of trying to show that the spontaneous order of capitalism is not only incredibly productive, but that it is able to produce optimal outcomes both on the level of the individual and society, where the latter is simply the sum of the former. Which is why in this universe if you know the motivations of the individual, you also know the aggregate results. A great shift took place in economic theory as marginalism transcended classical political economy. For what Walrasian theory claims is that a free market society best promotes the fulfilment of individual self-interest, whereas classical political economy only argues that by allowing enlightened self-interest to flourish, social progress is achieved (Patnaik, 2011, p. 5). Note, however, that in Smith, there is no claim that capitalism best fulfils the individuals self-interest, what Smith claims instead is, that if all agents strive towards their self-interest, independently of their struggles, we see an increase in the wealth of the nation (Patnaik, 2011, p. 5). In other words, the Smithian view is already a complex view, where actions of the individuals have a different, and in his view very positive, aggregate result. That is not to say, however, that the system caters to the whims of the individual's utility function, quite the opposite could be true! Smith made a complex argument in favour of capitalism, essentially saying that in spite of it being a system of *bellum omnium contra omnes*, the aggregate result of these struggles increase the material wealth of the nation, and is thus seen as being beneficial.

Now some people might agree with this assessment and some people might disagree, but at least it is honest and factually correct – capitalism has indeed been able to produce more goods than any other system in history by being able to harness the incredible power of enlightened self-interest as described by Smith. Whether you find the method by which this was done distasteful is up to you. The claim by neoclassical utilitarian calculus is different, what Walras and co want to convince us is that capitalism also makes us happy by making our utility functions flourish. Now this is an altogether different argument from the one made by Adam Smith, who makes no such bold claims about the well-being of the individual, his argument is simply that capitalism, for all its faults, increases the material wealth of nations. Smith, while giving

his opinion on the Manchester system, leaves the cost benefit analysis to the individual and her or his personal views. We immediately see why this could be a problem: some people might not agree that the increase in the wealth of nations, as Smith put it, is worth the price.

The reasons for employing neoclassical utilitarian calculus, firmly grounded in methodological individualism, is because there is no debate whether the system fulfils the desires of the individual or not. This is because there is no gap between the individual and society, the latter is simply a reflection of the motivations of the former. The difference between Keynes, Smith, Marx and modern analysis of complex systems could not be further apart. Despite this editorial, this journal is aimed at presenting works and points of view featuring all manner of methodological creatures. The idealistic aim of the journal is that by giving a venue where different points of view come together, we can come up with a better understanding of the economy and the society in general, through actual discourse on different levels, whether it be a discourse on methodology, pure theory, a contribution in ethics or empirical studies. We are the digital tower of Babylon, a house of all faiths, the Review of Economics and Economic Methodology, published by the Movement for Economic pluralism.

Yet in the end, we may well turn out to be a chimera, a unicorn or some other manner of non-existent mythical creature, for the Manchester system is far less enlightened than both Mr Keynes and Mr Piketty like to imagine. It is not simply that capitalism continuously fails to produce enough jobs and that it creates centralisation of wealth in the hands of the very few; even the composition of production, succumbs to its internal logic. As a direct consequence of these tendencies, a large part of the social product in the capitalist economies has to be diverted towards manufacturing consent and support for the existing social arrangement. Because in its normal functioning capitalism creates unemployment, poverty and disparities in wealth, it follows, *ipso facto* that institutions need to be in place, which can mitigate the effects of these tendencies. These institutions are endogenous to the system and change with it through time, depending on the specific historical circumstances.

The fact that capitalism needs an institutional superstructure to legitimize it represents an inefficient use of resources. These are resources used to keep in check the potential political instabilities which would endanger the future operation of the system. Obviously if one could limit the reasons for these instabilities in the first place, less

energy would have to go into socially unproductive activities. When we think about specific institutions that make up the superstructure, look no further than the state, which for most of its existence, has helped foster the *laissez-faire* system. We can go back to the old institutions of the Roman Empire that fall under the rubric of *panem et circenses*, bread and games, and see that these institutions are just as important in capitalism, as they were back then. Finally, the Manchester system has, for the most part, support amongst the professional class, by which I mean lawyers, social scientists and academia in general. And this is the main problem that I feel no amount of open discussion can resolve, because if you are a member of a class that receives the surplus product without having produced it, then you will be blind to its very existence and the process by which it came to be. Much like a modern-day Don Quixote, this publication aims at trying to transcend materialistic determinism, believing that a fruitful scientific discussion between different paradigms is not only possible but also necessary. Perhaps we are just Kantians foolishly hoping to escape the prisoner's dilemma, but with that being said, how can we hope to break out of this prison, if we don't even try?

1. Bibliography

1. Kalecki, M. (1943). Political Aspects of Full Employment. *The Political Quarterly*. 14(4).
2. Keynes, J. M. (2003). *The General Theory of Employment, Interest and Money*. A project Gutenberg eBook. Originally published in 1936.
3. Patnaik, P. (2009). *The Value of Money*. New York: Columbia University Press.
4. Patnaik, P. (2011). *Re-Envisioning Socialism*. New Delhi: Tulika Books.
5. Shaikh, A. (2016). *Capitalism, Competition, Conflict, Crises*. New York: Oxford University Press.
6. Stockhammer, E., Ramskogler, P. (2008). Uncertainty and Exploitation in History. *Journal of Economic Issues*, XLII(1).
7. Sušnik, U. (2016). *Economic Growth and Income Distribution in Modern Monetary Economies: The Importance of Expectations and the Role of Institutions*. Doctoral dissertation, Faculty of Economics, University of Ljubljana.

Taleb, N.N. (2016). The Most Intolerant Wins: The Dictatorship of the Small Minority. Found on <https://medium.com/@nntaleb/the-most-intolerant-wins-the-dictatorship-of-the-small-minority-3f1f83ce4e15#.1yynwngi2>.