“Collective and individual rationality: Maynard Keynes’s methodological standpoint and policy prescription”

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Abstract

In a world of partially overlapping and partially conflicting interests there is good reason to doubt that self-seeking behaviour at the micro-level will spontaneously lead to desirable social outcomes at the macro-level. Nevertheless, some sophisticated economic writers advocating a *laissez-faire* policy prescription have proposed various 'invisible hand' mechanisms which can supposedly be relied upon to 'educe good from ill'. Smith defended the 'simple system of natural liberty' as giving the greatest scope to the unfolding of God's will and the working out of 'natural', providential processes free of interference by 'artificial' state intervention – the expression not of divine order but of fallible human reason. Hayek, adopting a similar policy stance, based it in an evolutionary process in which those institutional forms best adapted to reconciling individual interests would, he believed, spontaneously be selected for in the inter-group struggle for survival.

Keynes shares the holistic approach of Smith and Hayek, but without their reliance on invisible hand mechanisms. If spontaneous processes cannot be relied upon to generate desirable social outcomes then we have to take responsibility for achieving this ourselves by establishing the appropriate institutional framework.

Keynes takes a historical view of the role of capitalism and analyses its pathology as rooted in what we would now refer to as a multi-player prisoners' dilemma. The paper draws out the significance of his methodological standpoint here. Keynes's policy standpoint assigns a critical role to his own class, the 'educated *bourgeoisie*' in the reform process he maps out. A distinction, but also an intimate connection, is highlighted between, on the one hand, micro-level individualism (the 'Manchester System'), and, on the other, the macro-level collective action ('planning') required to preserve it. Finally Keynes is considered in relation to the themes of *laissez-faire*, holism, reductionism, providentialism and the invisible hand.

I Introduction

In previous papers (Denis, 1996a, b, 1997, 1999a, b, 2000, 2002a, b), and in my PhD thesis (Denis, 2001), I have tried to show two things: Firstly, that in a world of partially overlapping and partially conflicting interests there is good reason to doubt that self-seeking behaviour at the micro-level will spontaneously lead to desirable social outcomes at the macro-level. And, secondly, that some sophisticated economic writers who would like us to rely on the spontaneous interaction of self-seeking agents, writers advocating a *laissez-faire* policy prescription, have proposed various 'invisible hand' mechanisms which can, in their view, be relied upon to 'educe good from ill'. Smith, I argued, defended the 'simple system of natural liberty' as giving the greatest scope to the unfolding of God's will and the working out of 'natural', providential processes free of interference by 'artificial' state intervention – the expression not of divine order but of fallible human reason. Hayek, adopting a similar policy stance, based it in an evolutionary process in which those institutional forms best adapted to reconciling individual interests would, he believed, spontaneously be selected for in the inter-group struggle for survival.

The purpose of the present paper is to cast a light on this issue from another direction by displaying an example of the policy consequences of adopting an alternative methodological stance. The argument of the paper is that (a) staying within the holistic methodological framework of Smith and Hayek, but (b) rejecting their invisible hand mechanisms, leads (c) to the rejection of their reductionist *laissez-faire* policy stance as well.

The structure of the paper is as follows. In Section 2 I show Keynes's view of the historical role of capitalism and his analysis of its pathology, rooted in what we would now refer to as the prisoners' dilemma. Section 3 draws attention to the fundamental significance of his methodological standpoint. This lays the basis for a consideration of his policy prescription in the following two sections. Section 4 looks at two very important aspects to the question, spelling out Keynes's call for planning, and explaining exactly what he meant by this. Before doing so however – and this is the other key aspect to the question – the section examines Keynes's *class* standpoint, showing the critical role he expected his own class, the 'educated *bourgeoisie*', to play in the reform process he mapped out. Section 5 adds a further layer to the consideration of Keynes's policy prescription, drawing out the distinction, but also the intimate connection, between, on the one hand, micro-level individualism (the 'Manchester System'), and, on the other, the macro-level collective action ('planning') required to preserve it. Finally, Section 6 concludes by considering Keynes in relation to the themes of the research of which this paper is part – Smith and Hayek, holism, reductionism and the invisible hand.

II Keynes's historical perspective

Whereas, for Smith and Hayek capitalist individualism is the terminus of an *ontogenetic* process, for Keynes it is something transitional, something with a historical and conditional validity. Keynes's historical perspective is thus consistent with a *phylogenetic* evolutionary stance. *Laissez-faire* in Keynes's conception performed a vital historical role, carrying us from an Era of Scarcity to an Era of Abundance. It was precisely because it had substantially fulfilled that role that it had become counter-productive. The point is controversial. Joan Robinson claimed that Keynes 'saw the capitalist system as ... a phase in historical development' (Robinson, 1964: 71); Geoffrey Pilling, on the other hand, criticising both Keynes and Robinson, writes that 'It is just this historical conception of capitalism which is absent in Keynes' (Pilling, 1986: 35, and n1). The purpose of this section is to show that Robinson was right, and Pilling wrong[1], on this point: to establish Keynes's conception of the historical role of capitalism – though not, I should emphasise, necessarily to defend it.

In order to establish Keynes's view of the historical and historically limited role of *laissez-faire*, we must say something about his conception of the historical context, that is, about his periodisation of history. I have attempted to reconstruct Keynes's view here by rereading 'Am I a Liberal?' (Keynes, 1925b) in the light of his later works, in particular 'Economic Possibilities for our Grandchildren' (Keynes, 1930c), and Book VI of the *General Theory*, 'Short Notes Suggested by the General Theory' (Keynes, 1973a: 313-384).

The first great era in Keynes's scheme takes in prehistoric, ancient and medieval times. In the 'Era of Scarcity' (Keynes, 1972a: 304) production is overwhelmingly production for the sake of consumption, indeed subsistence purposes: 'The economic problem, the struggle for subsistence, always has been hitherto the primary, most pressing problem of the human race – not only of the human race, but of the whole of the biological kingdom from the beginning of life in its most primitive forms' (Keynes, 1972a: 326-327). During the Era of Scarcity, there is an overwhelming obstacle to the accumulation of capital in the form of uncertainty driving the marginal efficiency of capital (*MEC*) below the rate of interest (*i*):

> "The destruction of the inducement to invest by an excessive liquidity-preference was the outstanding evil, the prime impediment to the growth of wealth, in the ancient and medieval worlds. And naturally so, since certain of the risks and hazards of economic life diminish the marginal efficiency of capital while others serve to increase the preference for liquidity. In a world, therefore, which no one reckoned to be safe, it was almost inevitable that the rate of interest … would rise too high to permit of an adequate inducement to invest." (Keynes, 1973a: 351)

At – so to speak – the other end of history from the era of scarcity, in the near future, lies 'our destination of economic bliss' (Keynes, 1972a: 331), 'economic paradise' (Keynes, 1972a: 268), 'the age of leisure and abundance' (Keynes, 1972a: 328). 'The economic problem may be solved, or be at least within sight of solution, within a hundred years ... the economic problem ... is not the permanent problem of the human race' (Keynes, 1972a: 326). The essence of the era of abundance is that 'needs are satisfied in the sense that we prefer to devote our further energies to non-economic purposes' (Keynes, 1972a: 326). Thus, we may note in passing, production here, too, is for the sake of consumption in the broadest sense: 'for the first time since his creation man will be faced with his real, his permanent problem – how to use his freedom from pressing economic cares …. to live wisely and agreeably and well' (Keynes, 1972a: 328).

The following year, in the Preface (dated 1931) to *Essays in Persuasion* (Keynes, 1972a), a collection of essays spanning a dozen years, this approaching liberation from economic care has become his 'central thesis throughout': 'the day is not far off when the economic problem will take the back seat where it belongs, and that the arena of the heart and head will be occupied ... by our real problems – the problems of life and human relations, of creation and behaviour and religion' (Keynes, 1972a: xviii). This messianic strand, though expressed in more sober language, still plays a central, and, indeed, even more urgent, role in the *General Theory*. The age of abundance now appears as the 'quasi-stationary community' (Keynes, 1973a: 220), and is to be attained, not in our grandchildren's time, but 'within a single generation' (Keynes, 1973a: 220), 'say within twenty-five years or less' (Keynes, 1973a: 324).

The modern period, the third historical division or 'economic order' (Keynes, 1972a: 304) in Keynes's schema, is the age of capitalism. This period does not have the fundamental, self-sufficient character of the other two epochs, but is simply the period of transition from the one to the other. As such it is not an end in itself but a means to an end lying beyond itself, namely our entry into the 'economic paradise'. Hence our judgement of capitalism must refer, not to how pleasant or otherwise it may be, but to its efficacy in achieving that end:

> "Many people, who are really objecting to capitalism as a way of life, argue as though they were objecting to it on the ground of its inefficiency in attaining its own objects … For my part I think that capitalism, wisely managed, can probably be made more efficient for attaining economic ends than any alternative system yet in sight, but that in itself it is in many ways extremely objectionable." (Keynes, 1972a: 294)

Capitalism achieves this end, in Keynes's view, by means of the accumulation of capital, and, for Keynes, the rate of capital accumulation is the measure of the rate of our approach to the economic paradise. To denote the motives to this accumulation of capital, Keynes spoke of 'compound interest' (Keynes, 1972a: 324) and 'purposiveness' (Keynes, 1972a: 329). By this latter peculiar expression, 'purposiveness', he merely means money-making as an end in itself, saving, ostensibly for future consumption, but actually for the sake of accumulating claims on future production; saving not in order to enjoy the deferred consumption later, but in order to secure a stream of unearned income. Keynes analyses 'purposiveness' psychologically as an attempt to gain immortality by projecting one's actions into an indefinite future by means of an infinite regress:

> "purposiveness means that we are more concerned with the remote future results of our actions than with their own quality ... the purposive man is always trying to secure a spurious and delusive immortality for his acts by pushing his interest in them forward in time." (Keynes, 1972a: 330)

Just as Marx, in the Communist Manifesto, for example, was outspoken in his praise for the achievements of capitalism (Marx and Engels, 1976: 489), Keynes, too, paid tribute to those achievements: 'In the nineteenth century this epoch culminated gloriously in the victories of *laissez-faire* and historic Liberalism.' (Keynes, 1972a: 304) The accumulation of capital depended upon the freedoms of *laissez-faire* – in particular, private properly in the means of production and unrestricted scope for the operation of market forces:

> "The system worked, throughout Europe, with an extraordinary success and facilitated the growth of wealth on an unprecedented scale. To save and invest became at once the duty and the delight of a class. The savings were seldom drawn on, and, accumulating at compound interest, made possible the material triumphs which we now all take for granted. The morals, the politics, the literature, and the religion of the age joined in a grand conspiracy for the promotion of saving." (Keynes, 1972a: 62)

In one of his essays on Liberalism, where he applied to his own views the term 'New Liberalism' (Keynes, 1972a: 305), he remarked that 'old-fashioned individualism and laissez-faire ... contributed to the success of the nineteenth-century ... I should have belonged to this party [sc the Liberal Party] if I had been born a hundred years earlier' (Keynes, 1972a: 300-301).

While recognising the historical necessity and legitimacy of the *laissez-faire* system, and appreciating the benefits of its 'material triumphs', Keynes nevertheless deprecated the subversion of morals he believed it involved: 'we have exalted some of the most distasteful of human qualities into the position of highest virtues.' (Keynes, 1972a: 329) Keynes is here protesting against the fact that capitalism requires, and *laissez-faire* permits, the transformation of the economy from production for the sake of consumption to production for the sake of profit, for the sake of the accumulation of wealth. Saving for the sake of future consumption Keynes can put up with; saving in order 'to exploit the scarcity value of capital' (Keynes, 1973a: 376) is morally reprehensible.

That mankind has had to depend on this sort of egoistic materialism in order to raise itself from scarcity to abundance had had, according to Keynes, widespread deleterious consequences. Defining capitalism as 'egotistic atomism', he complains that: 'modern capitalism is absolutely irreligious, without internal union, without much public spirit, often ... a mere congeries of possessors and pursuers' (Keynes, 1972a: 267). 'I think that Capitalism ... in itself is in many ways extremely objectionable' (Keynes, 1972a: 294).

> "[T]he moral problem of our age is concerned with the love of money, with the habitual appeal to the money motive in nine-tenths of the activities of life, with the universal striving after individual economic security as the prime object of endeavour, with the social approbation of money as the measure of constructive success, and with the social appeal to the hoarding instinct as the foundation of the necessary provision for the family and for the future." (Keynes, 1972a: 268-9)

The ultimate problem with Capitalism, however, was when it became ineffective as a means to the end which justified it: 'Capitalism ... is not intelligent, it is not just, it is not virtuous – and it doesn't deliver the goods' (Keynes, 1982: 239). Nevertheless, despite these criticisms of capitalism, Keynes was anxious not to throw out the baby with the bathwater:

> "It is common to hear people say that the epoch of enormous economic progress which characterised the nineteenth century is over … I believe this is a wildly mistaken interpretation of what is happening to us. We are suffering, not from the rheumatics of old age, but from the growing pains of over-rapid changes, from the painfulness of readjustment between one economic period and another." (Keynes, 1972a: 321)

The fundamental, underlying problem in this period is that production is not directly production for the sake of consumption, as it is in the two great eras of scarcity and abundance, instead we have production for the sake of profit, of accumulation, for the sake, that is, of production itself. A comparison of the category 'consumption' as it appears in 'Economic Possibilities for our Grandchildren' (Keynes, 1930c) with that in Keynes, 1973a shows it in two diametrically opposed rôles. Consumption today is consumption for production: it does not matter what it is consumption *of* so long as it contributes to aggregate demand and hence keeps the accumulation of capital going. In the future, in the 'economic paradise', production is a mere means, and consumption the end: in that context consumption means 'learning to live wisely and agreeably and well' (Keynes, 1972a: 328), solving 'the problems of life and human relations, of creation and behaviour and religion' (Keynes, 1972a: xviii). The critical importance of this view of consumption, and its methodological implications, will be taken up in the next section.

The problems of this period of 'capitalistic individualism' are for Keynes precisely those arising from its transitional nature. The *MEC* is falling precisely because it has fulfilled its purpose. Its purpose was to promote the accumulation of capital and, in general, the wealth of society: the falling *MEC* (and marginal propensity to consume, *MPC*) are the inevitable result of that accumulation. Indeed, for Keynes, the definition of the 'economic paradise' is that the *MEC* has fallen to zero. There is nothing pathological about this – on the contrary, it is to be expected and desired.

The trouble arises from the institutional context within which the transition was taking place, namely that of *laissez-faire*. Under *laissez-faire*, Keynes believed, and believed he had demonstrated, the *MEC* falls faster, and further, than the rate of interest (*i*). This is due to a peculiarity of money that it can act as a store of value for the individual but not for the community – what is true for each individual taken separately is not true for all the individuals taken together. '[T]here is no such thing as liquidity of investment for the community as a whole' (Keynes, 1973a: 155). If the community tries to convert part of its aggregate income into a hoard of money, total income simply declines to the point where the community no longer tries to do so.

Keynes's argument is that the natural tendency for the *MEC* to decline with increasing abundance of capital should be matched by an offsetting tendency for *MPC* to decline with increasing income. *i* should therefore decline *pari passu*: the opportunity cost of investment – that is, the foregone or postponed consumption – should fall to zero, since that portion of income is saved anyway. Given an adequate institutional framework this is what will happen. The *MEC* can then decline to zero without falling below *i* and hence without investment being brought to a standstill. Once the *MEC* has fallen to zero, capital goods are essentially free and we have entered the economic paradise.

However, the institutional framework is *not* adequate: the *laissez-faire* system introduces an intolerable level of uncertainty. If every agent were in some way linked up to every other so that they could act in concert, each would realise that it is in the interest of all to make sure that their saving and investment correspond. No-one could have any interest in a beggar-thy-neighbour policy of hoarding money. But *laissez-faire* means, precisely, that this coordination is lacking. *Laissez-faire* divides everyone from everyone else: it's every man for himself. Every agent must now be in ignorance as to what his fellows are going to do. Instead of assessing real economic conditions each agent must now devote himself to guessing what all the *other* agents think of those conditions, or, rather, to guessing what each other agent guesses every other agent guesses... A rational saver may know that it would be best for all if he (and everyone else) were to restrain himself from hoarding money; he may even assume that everyone else knows this in theory, but he cannot be certain that everyone will have the necessary restraint not to save money 'just in case'. Any such suspicion means that he would be well advised to increase the liquidity of his assets a little. But if he, as a rational agent, finds that necessary, then so presumably do other agents. Every increase in the demand for money as an asset, a store of value (or liquidity preference, as Keynes calls such demand), is a reduction in aggregate demand (*AD*). A reduction in *AD* means a fall in the *MEC*. The agent must now believe, correctly, that a severe economic recession is on the way, and would be foolish not to build up as large a pool of liquid wealth as possible, thereby driving up *i* yet further. Even if the agent is fully conscious that he is contributing to the crisis, exacerbating it, there is absolutely nothing that he, as an isolated individual, can do about it[2].

> "Many of the greatest economic evils of our time are the fruits of risk, uncertainty, and ignorance ... these ... factors are ... the cause of un-employment ... Yet the cure lies outside the operations of individuals; *it may even be to the interest of individuals to aggravate the disease*. I believe that the cure for these things ... would involve Society in exercising directive intelligence ... over ... private business." (Keynes, 1972a: 291-292; my emphasis)

The essence of the prisoners' dilemma (Denis, 1996a, 2001 Ch 2) is that the prisoners are compelled to pursue their partially overlapping and partially conflicting interests rationally but without collaboration. It shows how rationality at the individual (micro) level necessarily leads to irrationality at the collective (macro) level under these conditions. The essence of Keynesian opposition to *laissez-faire* is that by artificially dividing economic agents from each other it compels them, in individual self defence, to act in a manner detrimental to themselves as a group. Keynesian agents thus find themselves in what we in retrospect can see as a prisoners' dilemma. Not, indeed, a one-shot game, but an indefinitely repeated one. Players in an indefinitely repeated game may under certain circumstances – a sufficiently large probability of further rounds of the game together with a sufficiently low rate of discount of future payoffs – find their way to a cooperative outcome. However, while this is the case for two-player games, the achievement of such desirable outcomes rapidly becomes extremely difficult as the number of players rises above two. With any significant number of players, it becomes impossible to discriminate between cooperators and defectors, leading to the collapse of reciprocity: defection is once more the dominant strategy. And in the Keynesian case we have a multi-player game with the number of players being the number of wealth owners who need to determine the proportions of money and other assets to hold in their portfolios.

Keynes says something remarkable, in this connection, in his 'Notes on the Trade Cycle' (Keynes, 1973a: Ch 22: 313-332). The crisis, he says, is due to an 'error of pessimism' in which

> "the investments, which would in fact yield 2 per cent in conditions of full employment, are expected to yield less than nothing; and the resulting collapse of new investment then leads to a state of unemployment in which the investments, which would have yielded 2 per cent in conditions of full employment, in fact yield less than nothing." (Keynes, 1973a: 322)

Clearly this is not an 'error' on the part of the *individual* investors: they expected yields to fall by more than two percentage points and that is exactly what happened; their expectations were quite rational. The 'error' is on the part of the investors *as a whole*: it was sheer insanity for them to be pessimistic as it was precisely that pessimism which led to the collapse in new investments, the consequent unemployment and hence the collapse in yields. The institutional framework of *laissez-faire* dictates individual decision-making on an issue which is fundamentally not an individual matter.

Laissez-faire divides economic agents from each other and leads to uncertainty; uncertainty leads to increased liquidity preference; raised liquidity preference leads to recession; and recession leads to unemployment: 'A monetary economy ... is essentially one in which changing views about the future are capable of influencing the quantity of employment' (Keynes, 1973a: xxii). 'Unemployment develops ... because people want ... money' (Keynes, 1973a: 235). Because of this irreducible uncertainty associated with the *laissez-faire* system, Keynes believed that capitalism would settle down to a normal condition of under-employment equilibrium: 'Unemployment ... apart from brief intervals of excitement is associated – and in my opinion, inevitably associated – with present day capitalistic individualism' (Keynes, 1973a: 381). 'We oscillate ... round an intermediate position appreciably below full employment' (Keynes, 1973a: 254).

This outcome has two particularly deleterious consequences, other than the obvious one that unemployment and a fall in aggregate income is in no-one's interest. Firstly, the regular fall in the *MEC* towards zero, and what that is an index of, namely, the accumulation of capital up to the desired level of intensity, is broken off. For as long as *MEC* is below i, this process cannot continue. Hence our entry into the 'New Jerusalem', as Lambert (1963: 358) puts it, is postponed for as long as we remain in this rut of under-employment.

Secondly, and this is critical for Keynes, unemployment may lead to damaging, revolutionary changes, either in the direction of fascism or of communism: 'it is certain that the world will not much longer tolerate [this] unemployment' (Keynes, 1973a: 381). 'If [income deflation] occurs, our present regime of capitalistic individualism will assuredly be replaced by a far-reaching socialism' (Keynes, 1971: 346). On another occasion, he took comfort from a general willingness to drop the philosophy of *laissez-faire* for similar reasons to his own – fear that the existing institutions would otherwise be jeopardised. He could discern, he claimed, 'a general conviction that the stability of our institutions absolutely requires a resolute attempt to apply what perhaps we know to preventing the recurrence of another steep descent' (Keynes, in Hutchison, 1977: 65).

Keynes thus wants reform in order to forestall revolution. Only change can keep things the same. The next section examines in more detail Keynes's methodological holism which laid the basis for his policy prescription, and subsequent sections examine what Keynes believed had to change, what he wanted to remain the same, and how it should be done.

III Keynes and holism

In the previous section, I argued that, for Keynes, the underlying problem with capitalism was that production was not for the sake of consumption, but for the sake of production itself. To elucidate the relation between production and consumption in Keynes, we need to consider a number of passages from the *General Theory* and early drafts. In a draft chapter of the *General Theory* (Keynes, 1979), Keynes adopted Marx's formulae for simple commodity circulation and capitalist circulation, $C – M – C'$ and $M – C – M'$. The first formula says that a commodity, C, is exchanged for money, M, and the latter used to purchase another commodity, C'. The difference between C and C' is qualitative: they are different commodities. The second says that a quantity of money, M is invested in commodities, C, and the latter sold for a quantity of money, M', greater than the original quantity ($M' = M + \Delta M$, $\Delta M > 0$)[3]. The mistake of the classical economists[4], Keynes says, was to assume that money has the role only of means of exchange, as it does in simple commodity circulation, rather than store of value, as in the circulation of capital. In simple commodity production, production is still for consumption: the original commodity is produced in order to sell it and with the proceeds purchase the commodity desired for consumption. In capitalist production, the purpose of production is to augment the value of the capitalist's wealth, and consumption is reduced to a means to this end. In the one case, money is a convenience allowing the commodity owner to translate his commodity, produced only for the market, into the one he wants to consume. In the other, money is money capital, money is the goal and criterion of production.

> "Karl Marx … pointed out that the nature of production in the actual world is not, as economists seem often to suppose, a case of C – M – C', ie of exchanging commodity for money in order to obtain another commodity. That may be the standpoint of the private consumer. But it is not the attitude of *business*, which is a case of M – C – M', ie of parting with money for commodity in order to obtain more money." (Keynes, 1979: 81)

While the formula for the circulation of capital expresses the 'standpoint of business', and the structure of incentives under capitalism, in Keynes's view this involves contradictions: although we might behave as though production were carried out for its own sake, this cannot literally be true: 'capital is not a self-subsistent entity existing apart from consumption' (Keynes, 1973a: 106); 'the expectation of consumption is the only *raison d'être* of employment'(Keynes, 1973a: 211); 'consumption – to repeat the obvious – is the sole end and object of all economic activity' (Keynes, 1973a: 104). The point Keynes is insisting on here is that production has to be validated by consumption to *count* as production: output must be sold to convert it back into money, and, indeed, more money than was started with. The subordination of consumption to production implicit in classical *laissez-faire* capitalism sets up a continually re-emerging barrier to accumulation in the form of under-consumption and failures of aggregate demand.

Keynes's approach here illustrates the methodological significance of his critique of classical economists, from Ricardo to Pigou. For the individual household, 'the standpoint of the private consumer', we have $C – M – C'$: consumption is the immediate goal of economic activity. So does this mean that $C – M – C'$ is valid for society as a whole? That is what 'economists seem often to suppose'. But that is reductionist: it is saying that what is true of the parts is therefore true of the whole. '[T]he nature of production in the actual world' is the opposite: $M – C – M'$: economic activity is directed towards the accumulation of claims on future production.

This rejection of reductionism is evidenced over and over again in Keynes's writings. In the famous passage from the 'Preface' to the French edition of the *General Theory*, cited in Section 6 of the present paper, Keynes criticises the classical economists for erroneously 'extending to the system as a whole conclusions which have been correctly arrived at in respect of a part taken in isolation' (Keynes, 1973a: xxxii).

The same line of criticism is apparent in Chapter 2 of the *General Theory*. Here Keynes criticises Ricardo for focusing on microeconomic problems concerning relative prices and the allocation of resources between different uses, and his denial of the desirability, indeed possibility, of macroeconomic analysis of the level of economic activity as a whole. Keynes cites Ricardo's letter to Malthus of 9 October 1820:

> "Political economy you think is an enquiry into the nature and causes of wealth – I think it should be called an enquiry into the laws which determine the division of the produce of industry amongst the classes who concur in its formation. No law can be laid down respecting quantity, but a tolerably correct one can be laid down respecting proportions. Every day I am more satisfied that the former enquiry is vain and delusive, and the latter only the true objects of the science." (cited in Keynes, 1973a: 4)

Later in the same chapter he criticises the classical school for its reductionist approach to the wage bargain. Keynes sets out his famous 'two postulates of classical economics: that 'The wage is equal to the marginal product of labour', and that 'the utility of the wage when a given volume of labour is employed is equal to the marginal disutility of that amount of employment'. The first says that firms are optimising in the labour market, the second that households are. Keynes conceded the first but denied that the second held as a rule. Classical economists who assumed it to be true forgot, he claimed, firstly, that the relationship between real and money wages was different for the individual industry and the whole economy:

> "In the case of a change peculiar to a particular industry one would expect the change in real wages to be in the same direction as the change in money wages. But in the case of changes in the general level of wages … the changes in real wages associated with a change in money wages … is almost always in the opposite direction." (Keynes, 1973a: 10)

Keynes is clearly reiterating the point that the whole cannot be understood as the sum of its parts: the relationship between real and money wages is transformed as we change levels. Here, an increase in money wages in an isolated industry would also be an increase in real wages, as the aggregate price level is unaffected; when we come to industry as a whole, a change in output will, in Keynes's opinion, be associated with a rise in the price level, and a smaller rise in the level of wages: real wages will fall.

Secondly, according to Keynes – and this is really the same point made another way – the classical economists forgot that the principle, that unemployed workers can always underbid the employed and so bring supply and demand into equilibrium in the labour market, is 'intended … to apply to the whole body of labour and do[es] not merely mean that a single individual can get employment by accepting a cut in money-wages which his fellows refuse' (Keynes, 1973a: 11). The point is, that if one worker 'considered in isolation' were to accept a cut in wages, this would be relative to a given price level, which would remain unchanged by his actions – and so his, or her, real wage would decline in the same proportion as the money wage. The actions of a single worker, in an economy of any significant size, have a vanishingly small impact on the general price level. For the actions of the workers as a whole this is no longer true: an attempt to reduce the general level of money wages, via their impact on firms' marginal costs, would lead to reductions in the general price level of about the same magnitude, leaving real wages where they were (Keynes, 1973a: 12). Again, it is clear that Keynes is making a point about the relationship between phenomena at the system and substrate levels, and criticising the classical economists for failing to see it. At the substrate level, the general price level is a parameter, at the system level it is a variable.

Numerous further examples from Keynes could be cited. At the risk of labouring the point, just two more instances will be considered here, both from the *General Theory*.

In Chapter 19, on 'Changes in Money Wages', Keynes once again takes the 'classical economists' to task, in a passage of such clarity as to render exegesis redundant, for impermissibly transferring unexceptionable micro statements to the macro context:

> "In any given industry we have … the demand schedule for labour in the industry relating the quantity of employment to different levels of wages … This conception is then transferred without substantial modification to industry as a whole; and it is supposed by a parity of reasoning, that we have a demand schedule for labour in industry as a whole relating quantities of employment to different levels of wages … [S]urely [this] is fallacious. For the demand schedules for particular industries can only be constructed on some fixed assumption as to the nature of the demand and supply schedules of other industries and as to the amount of the aggregate effective demand. It is invalid, therefore, to transfer the argument to industry as a whole … But if the classical theory is not allowed to extend by analogy its conclusions in respect of a particular industry to industry as a whole, it is wholly unable to answer the question what effect on employment a reduction in money wages will have." (Keynes, 1973a: 258-260)

Finally, and for exactly the same reasons, we may note that in the chapter of the *General Theory* on 'The Theory of Prices' (Keynes, 1973a: Chapter 21, 292-309), Keynes rejects the classical dichotomy 'between the theory of value and distribution on the one hand and the theory of money on the other hand' (Keynes, 1973a: 293).

> "The right dichotomy is, I suggest, between the theory of the individual industry or firm and of the rewards and the distribution between different uses of a *given* quantity of resources on the one hand, and the theory of output and employment *as a whole* on the other hand." (Keynes, 1973a: 293)

Keynes is again clearly articulating a holist conception here. The classical dichotomy distinguishes between a real supply side and a purely nominal demand side – a standpoint which, as he points out, implies that at the macro level 'the elasticity of supply must have become zero and demand proportional to the quantity of money' (Keynes, 1973a: 292). This classical standpoint tacitly – and illicitly – assumes that what is '*given*' at the micro level, namely the quantity of resources which is employed in the economy as a whole, must also be given at the macro-level, the level to which monetary theory applies. This leaves money with no real effects (the real and monetary sectors are dichotomous): from our standpoint as observers it is a mere veil over the real workings of the economy. In opposition to this classical dichotomy, Keynes proposes his own micro-macro dichotomy: a micro sphere of analysis in which conclusions can be 'correctly arrived at in respect of a part … taken in isolation' (Keynes, 1973a: xxxii), and a macro sphere to be analysed as a whole, as a system, and in which money attains critical importance for real outcomes.

IV Keynes's policy prescription

The overview, in the previous two sections, of Keynes's dynamic and historical view of the pathologies of capitalism, and of his clear sighted articulation of the micro and macro levels in economics, lays the basis for an understanding of his policy prescription. Only one further point is required. In utter contrast to Smith's invisible hand of god, and Hayek's evolutionary theory of group selection, Keynes never for a moment assumes that we live in a world endowed with providential, pro-human qualities. His standpoint is entirely consistent with that of A.E. Houseman's 'heartless, witless Nature' (cited, Dawkins, 1995:155). If good is to be found in the world, it must be the result of our own activity. In such a world, a policy of *laissez-faire* is a non-starter.

So what was Keynes's policy prescription – and, moreover, who was to execute it? A careful reading of Keynes makes it quite clear what he was prepared to sacrifice, and what he was determined at all costs to retain – what it was about 'our institutions' and 'the kind of system in which we actually live' (Keynes, 1973a: 247) which he thought worth keeping. What Keynes was concerned to defend was the liberties, the privileges, the prestige, the security, the standard of living, and in short the whole mode of life of the class of which he was a member: 'If I am going to pursue sectional interests at all, I shall pursue my own. When it comes to the class struggle as such ... the *Class* war will find me on the side of the educated *bourgeoisie*' (Keynes, 1972a: 297). Far from expressing any narrow, sectarian point of view, however, Keynes was able to take this stance because of the *universality* he ascribed to his class. As we shall see, the 'educated bourgeoisie' was a universal class in the sense that, by following its own interests, it would lead the whole population to the destination of economic 'bliss'.

The 'educated bourgeoisie' comprised for Keynes all those sections of society that his own activities made him part of – business management and public administration, and the worlds of academia and the arts. It excluded the actual owners of the means of production, the rentier capitalists, and it excluded the 'ordinary' people who 'sell themselves for the means of life' (Keynes, 1972a: 328). Keynes invented a rather grotesque *raison d'être* for this stratum, which runs as follows. The big problem with the approach of the 'economic paradise' is that *ordinary* people will not know what to do with themselves:

> "I think with dread of the adjustment of the habits and instincts of the ordinary man, bred into him for countless generations, which he may be asked to discard within a few decades ... must we not expect a general 'nervous breakdown'?" (Keynes, 1972a: 327) "There is no country and no people, I think, who can look forward to the age of leisure and abundance without a dread ... It is a fearful problem for the ordinary person, with no special talents, to occupy himself ..." (Keynes, 1972a: 328).

Fortunately, however, there are strata of the population who are not 'ordinary', who do have 'special talents'. (These 'talents', however, turn out to be of the monetary variety.)

> "It will be those people, who can keep alive, and cultivate into fuller perfection, the art of life itself, and do not sell themselves for the means of life, who will be able to enjoy the abundance when it comes ... the wealthy classes in any quarter of the world ... are, so to speak, our advance guard – those who are spying out the promised land for the rest of us and pitching their tent there ... those who have an independent income but no associations or duties or ties" (Keynes, 1972a: 328).

Keynes immediately takes the opportunity of castigating the *idle* rich, the rentiers: 'most of them have failed disastrously ... to solve the problem which has been set them' (Keynes, 1972a: 328). Keynes is attacking them for failing to live up to the role he ascribes to the rich – the development of a good life of culture and consumption, rather than 'purposiveness' and hoarding – and thereby undermining the *raison d'être* of the class system. Keynes's attitude towards the rentier class is ruthless. If they will not spend their money, take it off them. He regarded the inheritance of fortunes as a specially pernicious, feudal institution, and favoured high death duties to counter its effect on the *MPC* (Keynes, 1972a: 299; Keynes, 1973a: 95, 372-3; Keynes, in

Hutchison, 1977: 72). Meanwhile, to the rest of us he addresses an appeal for another chance: ‘I feel sure that with a little more experience we shall use the new-found bounty of nature quite differently from the way in which the rich use it today, and will map out for ourselves a plan of life quite otherwise than theirs’ (Keynes, 1972a: 328).

Keynes’s belief in the importance of class distinctions comes out clearly when he states his differences from communism :

> “How can I adopt a creed which, preferring the mud to the fish, exalts the boorish proletariat above the *bourgeois* and the intelligentsia who, with whatever faults, are the quality in life and surely carry the seeds of all human advancement ... It is hard for an educated, decent, intelligent son of Western Europe to find his ideals here ... It exalts the common man and makes him everything.” (Keynes, 1972a: 258-259)

We should be quite clear, here, what Keynes means by the *bourgeoisie*. Just as he borrowed the designation ‘classical economists’ from Marx and then proceeded to use it in a completely different – almost opposite – sense[5], his use of the term bourgeois has little or no overlap with Marx’s conception of the capitalist class. The ‘educated bourgeoisie’, the ‘bourgeoisie and intelligentsia’, in Keynes do not include the owners of the means of production, the capitalists *per se* (whether holders of debt or equity). When he explicitly sides with the bourgeoisie, by no means is Keynes erecting an apology for the rentier. The latter he regards as a parasitic excrescence on the productive apparatus of society, and one which is in the course of quiet liquidation by the spontaneous development of the economy itself:

> “The rentier aspect of capitalism [is] a transitional phase which will disappear when it has done its work ... the euthanasia of the rentier, of the functionless investor, will be nothing sudden, merely a gradual but prolonged continuance of what we have seen recently in Great Britain, and will need no revolution.’ (Keynes, 1973a: 376)

This particular terminology adopted by Keynes means that when he speaks of ‘private initiative and responsibility’, ‘the traditional advantages of individualism’, ‘personal liberty’, and so on, as desirable attributes of capitalism which will be retained in the new society (Keynes, 1973a: Ch 24 passim), he is not referring to private property in the means of production. Indeed, the question of private or public ownership of the means of production was a non-issue as far as Keynes was concerned:

> “It is not the ownership of the instruments of production which it is important for the state to assume.” (Keynes, 1973a: 378) “There is no so-called important political question so really unimportant, so irrelevant to the reorganisation of the economic life of Great Britain, as the Nationalisation of the Railways.” (Keynes, 1972a: 290)

Nationalisation was a non-issue for Keynes because the ‘educated bourgeoisie’ was in fact taking, or had already taken, control of the bulk of industrial – and, indeed, non-industrial – institutions. This theme in Keynes – the separation of ownership and control, leading to the hegemony of the managers in industry and state – has since become a major tradition in its own right. The theme originally had two aspects, distinguishing between holders of debt and equity. In 1923 Keynes described what he calls ‘the Investment System’, in these terms:

> “Under this phase of capitalism, as developed during the nineteenth century, arrangements were devised for separating the management of property from its ownership ... Contracts to receive fixed sums of money at future dates must have existed as long as money has

> been lent and borrowed ... But during the nineteenth century they developed a new and increased importance, and had, by the beginning of the twentieth, divided the propertied classes into two groups – the 'business men' and the 'investors' – with partly divergent interests ... business men might be investors also, and investors might hold ordinary shares; but the division was nevertheless real." (Keynes, 1972a: 61-62)

The second phase, so to speak, occurs when the rentiers, or 'investors', buy up the shares, too, and leave the managers without any ownership stake in the enterprise.

> "A point arrives in the growth of a big institution ... at which the owners of the capital, ie the shareholders, are almost entirely dissociated from the management, with the result that the direct personal interest of the latter in the making of great profit becomes quite secondary." (Keynes, 1972a: 289)

Keynes calls this 'the tendency of big business to socialise itself' (Keynes, 1972a: 289), and describes it as 'a natural line of evolution. The battle of Socialism against unlimited private profit is being won in detail hour by hour' (Keynes, 1972a: 290). A salient example cited by Keynes in this context, and – significantly – prior to its nationalisation, is that of the Bank of England: 'there is no class of persons in the kingdom of whom the Governor of the Bank of England thinks. less when he decides on his policy than of his shareholders. Their rights, in excess of their conventional dividend have already sunk to the neighbourhood of zero' (Keynes, 1972a: 290).

This conception of what has since been sensationalised as a 'managerial revolution' is crucial to the understanding of Keynes's policy prescription. Keynes's aim is an adequate policy framework for '[t]he transition from economic anarchy to a regime which deliberately aims at controlling and directing economic forces' (Keynes, 1972a: 305). He wants 'a somewhat comprehensive socialisation of investment' (Keynes, 1973a: 378); he wants 'planning' (Keynes, in Hutchison, 1977: 72, 77); he wants, as he told Hayek, 'more planning' (Keynes, 1980: 387). He was enthusiastic about the proposals for a national plan contained in the Mosley Manifesto (Keynes, 1930b). 'The central debate in politics, he [sc Keynes] wrote, was between planning and laissez-faire' (Skidelsky, 1975: 241).

But what sort of planning does Keynes want? Planning by whom? For whom? We have already seen his contempt for 'the ordinary man with no special talents', and for 'the mud ... the boorish proletariat' who 'sell themselves for the means of life'. He is even less sympathetic towards those at the opposite pole of the social spectrum. Keynes clearly believed that the 'beastly', 'avaricious' Jews were over-represented, to put it no more strongly than that, among the rentier capitalists. He writes in 'A Short View of Russia' (Keynes, 1925a) that 'the mood of oppression ... in Russia ... is the fruit of some beastliness in the Russian and Jewish natures ...' (Keynes, 1972a: 270), and in the same article remarks that the Russian Revolution has failed to make the Jews any less avaricious (Keynes, 1972a: 259). In a highly sinister passage, Keynes daydreams about the fate of Jewish financiers in the economic paradise to come:

> "The love of money as a possession ... will be recognised for what it is, a somewhat disgusting morbidity, one of those semi-criminal, semi-pathological propensities which one hands over with a shudder to the specialists in mental disease ... Perhaps it is not an accident that the race which did most to bring the promise of immortality into the heart and essence of our religions has also done most for the principle of compound interest and particularly loves this most purposive of institutions." (Keynes, 1972a: 329-330)[6]

Keynes's vision of planning, therefore, is one in which the main role is taken by the 'educated bourgeoisie', excluding the 'common people' on the one side, and the (mainly Jewish) rentiers on the other. While expressing no particular desire to dispense with parliamentary democracy, he clearly regards it as simply irrelevant: 'in the future the Government will have to take on many duties which it has avoided in the past. For these purposes Ministers and Parliament will be unserviceable' (Keynes, 1972a: 301-302).

So, in answer to the question of what it is that Keynes wants to preserve in 'existing economic forms', what he means when he refers to the preservation of 'individual initiative' and its 'successful functioning' (Keynes, 1973a: 380), I have argued that Keynes is anxious, above all, to preserve the status and privileges of his own class, the 'educated bourgeoisie', the 'advanced guard ... spying out the promised land'. It is *their* 'individual initiative' which he wishes to defend. 'Private self interest', expressed through consumer preferences on the market, and the exercise of 'enterprise and skill in the estimation of prospective yields' (Keynes, 1973a: 221) on the part of the entrepreneur, 'will determine what in particular is produced, in what proportions the factors of production are combined to produce it, and how the value of the final product will be distributed between them' (Keynes, 1973a: 379). Just as when Smith and Hayek speak of the rights of 'the individual' they refer to the individual owner of wealth, the individual as vehicle for capital, and in every other context the individual is the servant of 'society' (Denis, 1999b, 2001 Ch 5), so for Keynes the 'individual' who is truly efficacious, who enjoys freedom, opportunity and activity, is the 'educated *bourgeois*', the gentleman of independent means and public spirit.

It seems fair to summarise Keynes's vision of planning as a network of 'semi-autonomous bodies' – quangos and quagos linked together and to the national bank by a board of public investment:

> "Progress lies in the growth and the recognition of semi-autonomous bodies within the state ... bodies which in the ordinary course of events are mainly autonomous within their prescribed limitations, but are subject in the last resort to the sovereignty of the democracy expressed through Parliament." (Keynes, 1972a: 288-289)

Now, even the private enterprise firms of the *laissez-faire* period were 'in the last resort' subject to parliamentary sovereignty. To say this of the 'semi-autonomous bodies' is to say very little. In practice, what we have is a new *laissez-faire*, differing from the old in being collective rather than individualistic. The managerial class, which has quietly triumphed in both the formally private and the formally public sectors, is to be allowed to get on with it, free – in the ordinary course of events – of effective parliamentary supervision, regulation or restraint.

Keynes's articles in *The Times* in January and March, 1937, provide perhaps the most explicit statement of how these 'semi-autonomous bodies' are to be linked, as well as a useful ostensive definition of 'semi-autonomous body':

> "Now is the time to appoint a board of public investment ... to make sure that detailed plans are prepared. The railway companies, the port and river authorities, the water, gas and electricity undertakings, the building contractors, the local authorities, above all, perhaps, the London County Council and the other great corporations with congested population, should be asked to investigate what projects could be usefully undertaken if capital were available at certain rates of interest – 3½%, 3%, 2½%, 2%. The question of the general advisability of the schemes and their order of preference should be examined next. What

> is required at once are acts of constructive imagination by our administrators, engineers, and architects, to be followed by financial criticism, sifting and more detailed designing." (Keynes, in Hutchison, 1977: 72)

This is one half of the strategy. The other half is to ascertain from the mass of information obtained in this, and every other conceivable way, what rate of interest would be compatible with a flow of new projects just sufficient to absorb what the nation chooses to save:

> "The rate of interest must be reduced to the figure that the new projects can afford. In special cases subsidies may be justified. But in general it is the long-term rate of interest which should come down to the figure which the marginal project can earn ... We have the power to achieve this. If we know what rate of interest is required to make profitable a flow of new projects at the proper pace, we have the power to make this rate prevail in the market." (Keynes, in Hutchison, 1977: 73)

There are three points worth noting here, as to why Keynes is so confident about the rate of interest, when, after all, he had only recently proclaimed himself 'somewhat sceptical of the success of a merely monetary policy directed towards influencing the rate of interest' (Keynes, 1973a: 164).

The first point is that the Bank of England had already been cited by Keynes as a progressive example of 'semi-autonomous body', and of course the Treasury consists entirely of administrators and economists. The two institutions could therefore be depended upon, once Keynesian ideas had made themselves felt, to take the side of the 'educated bourgeoisie' against the rentiers, on the one side, and against interference by the electorate via parliament, on the other.

The second point is that due to the institutionally powerful position in the market of the Treasury and central bank, 'it lies within their power ... to make the long-term rate of interest what they choose within reason' (Keynes, in Hutchison, 1977: 73). The channelling of savings through the national bank, too, would give the state additional leverage against the rentier class and undermine the ability of the latter to dictate absolutely the rate of interest on borrowed capital (Keynes, in Hutchison, 1977: 73, Keynes, 1973a: 376).

Thirdly, the plan has been drawn up by the business community themselves, and in a collective rather than individualistic way. Everyone knows what the rest of the economy is doing and no-one has any incentive to increase his liquid reserves. Consequently, there is nothing to force i up above MEC at full-employment. Uncertainty has been eliminated at the outset by removing the artificial isolation of economic agents imposed by the anachronistic *laissez-faire* approach to policy. The payoffs to holding money and bonds have been changed so that the prisoners' dilemma has been removed.

V Did Keynes reject *laissez-faire*?

So, did Keynes rejected *laissez-faire*? In the past three answers have been given – *yes*, *no*, and *yes and no* – all of them false. The first has tended to be associated with more left-wing interpreters of Keynes, such as Joan Robinson, and the second both with more conservative interpreters, and with left-wing anti-Keynesians, such as Geoffrey Pilling. The third alternative, that Keynes was inconsistent in his attitude to *laissez-faire*, has been a very common one, and in the 1930s cartoons used to appear in the press of

Keynes as a double-jointed man supporting, for example, both free-trade and protection.

These approaches fail to do Keynes justice. It is true that Keynes did not make the final break with classical economic theory until around 1933, and he himself aptly summarised his life to this point as ‘a long struggle of escape’ (Keynes, 1973a: xxiii). In spite of this, his general social and political philosophy was consistent throughout his productive life and, I would argue, the changes in his economic theory were designed specifically to supply a theoretical underpinning for his political attitudes: ‘The field of social philosophy is the field in which Keynes remained consistent throughout his career’ (Lambert, 1963: 344).

> “While the *General Theory* marks a sharp break in economic theory, the ‘social philosophy’ implications he drew from the work [in Chapter 24] are consistent with his earlier views. In fact the *General Theory* can be viewed as giving an economic theoretic rationalisation for views that Keynes’s ethics and intuition had led him to.” (Minsky, 1975: 145)

While they can thus agree that Keynes was consistent, commentators are anything but agreed on what it was that Keynes was (supposedly consistently) saying: ‘Keynes [is] essentially an economic liberal arguing for specific non-liberal measures solely in periods of unemployment’ (Corry, 1978: 26). ‘When the whole question of seeing that potential savings are not run to waste in unemployment … is added to the *agenda* [of government], it seem as if there is precious little *non-agenda* left’ (Robinson, 1964: 81).

The reason why these views are mistaken is that they take the supposed Keynesian rejection of *laissez-faire* (whether they assert or deny that rejection) to be a rejection *a limine*. It is not. An implication of the present paper is that it is a *critique* – a concrete negation with a concrete result. Keynes’s view of *laissez-faire* is not absolute but conditional and historical. His call for state intervention to equilibrate saving and investment is, in his own view, by no means timelessly or universally valid.

The difference between himself on the one hand, and, on the other, the old-fashioned Liberals as well as the classical school whose theories underlay the *laissez-faire* approach, was that Keynes ‘explained the phenomena, which the old Liberal school attributed to the unchanging and universal character of natural law, in terms of positive and therefore changeable laws and of the particular conditions obtaining at a given time and a given place’ (Lambert, 1963: 345).

Lambert here is commenting on Keynes’s first book, *Indian Currency and Finance* (1913), written when Keynes was still, in terms of economic theory, entirely within the neoclassical school. The point is that even where, as in his work prior to World War I, Keynes obtained results formally consonant with the neoclassical and liberal traditions, such as the correctness of the *laissez-faire* approach to the economic policy framework in the nineteenth century, these results were obtained on the basis of a different, more concrete and more historical methodology. It was this methodology which enabled him to develop a *vision* of what was wrong with *laissez-faire*, when his contemporaries could only see that *something* was wrong (Pigou, for example, in the 1930s), and hence enabled him to develop a theoretical account of the economic problems of his time.

* * *

> "Whilst, therefore, the enlargement of the functions of government involved in the task of adjusting to one another the propensity to consume and the inducement to invest, would seem to a nineteenth- century publicist or to a contemporary American financier to be a terrific encroachment on individualism, I defend it, on the contrary, both as the only practicable means of avoiding the destruction of existing economic forms in their entirety and as the condition of the successful functioning of individual initiative." (Keynes, 1973a: 380)

This passage, from the final chapter of the *General Theory*, is a concise statement of Keynes's rejection of *laissez-faire*. Yet taken out of context, it could be extremely misleading. The 'enlargement of the functions of government' does, it is true, include an expansion in the role of the existing state. This is concerned principally with the adjustment of the propensity to consume by manipulation of the rates of income tax and death duty, and by deciding how sharply progressive should be the former, channelling savings through a national savings bank, and a programme of emergency public works in severe recessions.

But this is not the main point for Keynes. His goal is not simply an 'enlargement of the functions' but a change in the *nature* of the state. What he wants is an extra- or non-parliamentary state consisting of a central bank and a national planning board linking together the enterprises (in the broadest sense) of the country into a single organisation. This organisation would, through discussion, draw out a consensus of the whole of the 'educated bourgeoisie'; there would be no call for compulsion. The cancellation of the artificial separation and atomisation of the 'entrepreneurs' (that is, the managerial class), by the principles of *laissez-faire*, would eliminate the uncertainty which gives rise both to damaging fluctuations in economic activity and to the under-employment equilibrium around which the economy oscillates.

This, then, is how a theory can be simultaneously 'revolutionary' (Keynes, 1935) and 'moderately conservative' (Keynes, 1973a: 377) in its implications. The (revolutionary) introduction of central controls and planning to achieve full employment at the macro level is to provide the necessary environment in which the (conservative) micro-level 'Manchester system' comes into its own' (Keynes, 1973a: 378-379). Keynes wants to combine micro-level individualism with the macro-level planning required to preserve it. To put it another way, individual self-seeking behaviour at the micro level will generate desirable social outcomes at the macro level when the institutional framework ensures that the payoffs to individual actions are such as to avoid prisoners dilemmas.

The transition from the Era of Scarcity to the capitalist epoch required central controls on production and distribution to reduce uncertainty and the rate of interest, and raise the marginal efficiency of capital. This was the age of mercantilism and absolutism. Now, in the period of transition from capitalism to the 'economic paradise', similar problems call for similar solutions: a latter-day mercantilist policy (Keynes, 1973a: Chapter 23), 'promoted by an authority unlikely to be superseded' (Keynes, 1973a: 203).

VI Conclusion: Keynes and providentialism

In a holist view of the world, the individual agents composing an economic system are, and are *primarily*, components of a social totality: their life process is determined by their mutual relations, the totality of which is the economic system. Under capitalism, however, the individual agents are divorced from each other and their relations are refracted through their sole link with society: the money nexus. This gives them the appearance of independent, asocial, biological totalities, and hence gives the real social totality the appearance of a mere *congeries*.

It is in a sense immaterial where the economist commences his study of society, whether he 'starts' from the part and deduces therefrom the nature of the whole, or *vice versa*. Friedman, for example, correctly observes that both he and Keynes work 'from the top down', while many monetarists and Keynesians work in the opposite direction (Friedman, 1976: 316). That makes no difference: what matters is not where you 'start' but where you end up: do you understand the economy as a totality – with Keynes, Marx, Hayek, and Smith – or as a congeries – with Friedman, Lucas, and the neoclassical school.

Reductionism is implicit in the 'classical' methodology that Keynes criticised, as well as the methodology of those neoclassical writers, such as Friedman, who re-assert the claims of pre-Keynesian economics post-Keynes. The agent is a rational, utility-maximising being; since society is merely a mass of like individuals, the results of the analysis of his behaviour can be applied directly to society as a whole. Thereby the latter is shown to be a rational, welfare-maximising aggregate of many individuals. Protracted, general, involuntary unemployment is not possible: no rational individual would under-utilise scarce resources, so humanity in the aggregate must necessarily be just as rational. On the other hand, the *appearance* of unemployment can be explained away as *false* appearance concealing the intrinsic rationality of the system: irrationality on the level of the system cannot be the fault of the system but only of the individuals comprising it – so apparent unemployment must in fact be voluntary, caused, for example, by wage rigidity or other micro-irrationality.

Keynes, summarising his whole approach in a passage to which I have already drawn attention, goes straight to the heart of this question:

> "I have called my theory a *general* theory. I mean by this that I am chiefly concerned with the economic system as a whole … And I argue that important mistakes have been made by extending to the system as a whole conclusions which have been correctly arrived at in respect of a part taken in isolation." (Keynes, 1973a: xxxii)

Keynes is saying that the principal *differentia* of his method from that of the 'classical economists' is that the system as a whole cannot be considered as a mere congeries of individuals 'taken in isolation'. This is so because those individuals *are not isolated* from each other: what one does affects others. An individual's decision to save or to invest or to hold money, for instance, has consequences for other individuals who are not party to the relevant transaction and hence unable to affect its outcome.

In this clash between the private form and public consequences of the decisions to consume, and to save, to hold money and to invest, we see again the combination of independence in form and interdependence in content of those decisions, which lies at the heart of the prisoners dilemma (Denis, 1996a, 2001 Ch 2). Keynes sees this clash between private action and public consequence as remediable only by the removal of the anachronistic private form of decision-making. Hence Keynes's opposition to *laissez-faire* and his demands for social control of the propensity to consume, for the 'comprehensive socialisation of investment', and for 'communal saving through the agency of the state' (Keynes, 1973a: 378, 376).

Keynes's holism lies essentially in this: were the community as a whole, or some state agency representing it, to control saving and investment, there would need never be any discrepancy between the two. The desirability of the marginal unit of investment would be equal to the sacrifice involved in the marginal unit of saving, and with the accumulation of wealth, both would decline to zero.

The problem is the presence of an anachronistic institutional framework – *laissez-faire* – which fragments the decision-making process without mitigating the social consequences of the decisions made. The *community* can only do *two* things with its income: consume it or invest it. The individual acting on the basis of self-interest, however, has third alternative: he can hoard part of his income as money. Indeed, if he foresees any slackening of aggregate demand, he would be unwise not to, even if he realises the damage he will inflict on the economy thereby: 'Every act of saving involves a 'forced' inevitable transfer of wealth to him who saves, though he in his turn may suffer from the saving of others.' (Keynes, 1973a: 212) Hence hoarding, which is the cause of the economic disease, is the rational response of individuals to the fear of that disease: 'It may even be to the interest of individuals to aggravate the disease.' (Keynes, 1972a: 318). Though in practice the matter might be highly complex, the solution is in principle simple: that individuals should act no longer as individuals but as a collectivity, in so far as *quantitative* investment decisions are concerned.

* * *

The assumption standing behind pre- and post-Keynesian mainstream economics is that the unintended consequences of individual actions are *essentially* benign. This providential assumption pervades the writings of Smith and Hayek, Friedman and Lucas. Keynes devoted his theoretical life to the demonstration that unintended consequences, just because they *are* unintended, are uncontrolled and liable to be thoroughly malign:

> "The world is *not* so governed from above that private and social interests always coincide … It is *not* a correct deduction form the principles of economics that enlightened self-interest always operates in the public interest." (Keynes, 1972a: 287-288) "There is no design but our own … the invisible hand is merely our own bleeding feet moving through pain and loss to an uncertain … destination." (Keynes, 1981: 474)

Keynes's rejection, in these passages, of providentialism and the invisible hand bring us full circle. The episodes in the history of economic thought considered in Denis (2001) have shown that the combination in decision-making of independence in form and interdependence in content is an issue which continually re-emerges in political economy. At every stage there is a clash between the scientific and the vulgar, the desire to understand and explain, on the one hand, and fear of the consequences of doing so, on the other. Providentialism plays a key role here.

In Denis (2001) I focused on two sophisticated attempts to underpin a reductionist *laissez-faire* policy prescription with a holistic methodology. Smith and Hayek, though separated by two centuries, have proposed very similar invisible hand mechanisms to mediate between the holistic nature of the world and the reductionist character of their desired policy framework. Consideration of Keynes has shone a light on their attempts: his account gives us an outstanding example of the fate of *laissez-faire* political economy if a holistic approach is not supplemented with the *deus ex machina* of an invisible hand.

The precise content of Keynes's escape from the twin *laissez-faire* strategies of reductionism, on the one hand, and holism plus an invisible hand, on the other, is perhaps of less interest than its existence. Keynes had a particular view of the class of which he was part – he saw it as a universal class in a Hegelian sense, leading humanity from darkness into light. He was also, in my reading, a virulent racist with very strong, deeply ambiguous feelings about Jews.[7] I believe that all of this shaped and coloured his reading of writers such as Ricardo and Marx, his positive analysis, and his policy prescription. So from the perspective of this paper, the details are less important than the fact that he showed that there was an escape route: the economy is to be studied as a system and not as a congeries, and our default is to act, not to do nothing. Against the atomism of the 'classical' economists he argues for a clear, holistic, systems view, and against the providentialism of the invisible hand theorists he simply and clear-sightedly denies that any such providential mechanism exists, and shows in detail the implications, positive and normative, of that denial.

So for Keynes, the invisible hand ensuring that desirable social consequences flow from self-seeking individual behaviour is a myth: but the job it was supposed to do, the reconciliation of partially conflicting and partially overlapping interests, still needs to be done. This reconciliation is to be achieved in Keynes's view by the universal class, the educated bourgeoisie, and, in particular, by the extra-parliamentary state which it will build, based around a board of national planning linking all the enterprises of the country to the central bank. For Keynes it is precisely the educated bourgeoisie which will take the place of the invisible hand.

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Notes

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[1] It has been argued (Geoffrey Kay, personal communication) that both Robinson and Pilling were right, here, since they meant different things by 'historical'. However, Pilling clearly believed he was talking about the same thing as Robinson and that she was wrong: 'One cannot … accept Joan Robinson's confident assertion about Keynes' – ie the assertion that Keynes viewed capitalism as a phase in historical development (Pilling, 1986: 57). On this latter point Pilling was clearly wrong and Robinson right. However, one might wish to go further and argue that there was a sense in which Pilling was right about Keynes being unhistorical because he, Keynes, had a notion of capital which was in some sense timeless.

But this goes beyond the question of whether Keynes had a historical view of capitalism, and slides over into another question, namely whether he had what one believes to have been the *correct* historical view of capitalism. That is not an issue I am addressing here.

[2] In the context of a discussion of different forms of the prisoners' dilemma Douglas Hofstadter has introduced a concept of 'reverberant doubt' which describes exactly what Keynes is concerned with here: 'Isn't this an amazing and disturbing slide from certain restraint ... It is a cascade, a stampede, in which the tiniest flicker of doubt has become amplified into the gravest avalanche of doubt. That is what I mean by 'reverberant' doubt' and one of the annoying things about it is that the brighter you are, the more quickly and clearly you see what there is to fear' (Hofstadter, 1985: 753).

[3] In Marx, the second formula is true of merchant capital, which buys cheap in one market and sells the same commodities dear in another market; in capitalist production proper the original money capital is invested in means of production – constant and variable capital (c, v) – which are then consumed in the process of production, generating new commodities which are subsequently sold for more than the value of the means of production: M – C: MP (c, v) … P … C' – M' (Marx, 1974: 25).

[4] Throughout this paper, the term 'classical' follows Keynes's usage, not Marx's. See next footnote.

[5] For Marx, 'classical' political economy referred to scientific economics – ie economics which, he felt, tried to explain, rather than to explain away, the nature of capitalistic production – from Petty in the late 17th century on, and culminating in Smith and Ricardo. Subsequent mainstream economists Marx designated 'vulgar', and considered to be only interested in explaining away the undesirable features of capitalism. Marx, however, explicitly noted Ricardo's acceptance of Say's Law as an apologetic and vulgar element 'unworthy' of his otherwise classical and scientific approach. For Keynes, on the contrary, 'classical' economists are precisely those mainstream economists, since Ricardo, who, like Ricardo himself, adopt Say's Law: he names JS Mill, Marshall, Edgeworth and Pigou as examples (**GT**: 3). Hence, for Keynes, the labour theory of value of Smith and Ricardo is 'pre-classical' (**GT**: 213).

[6] It should, I think and hope, be clear that presenting my interpretation of economists' writings implies no endorsement of their stance, but so that there should be no possibility of misinterpreting my motives in reporting Keynes's views here, I completely dissociate myself from his racist remarks and standpoint regarding supposedly 'avaricious' Jews and 'boorish' proletarians alike.

[7] This was mixed up in his mind with sexual questions – passages in his essays on Einstein and Dr Melchior being particularly remarkable expressions of this potent mixture of racial and sexual issues. It would be inappropriate, however, to develop this theme further here.