

## POST-KEYNESIAN POLITICS AND THE POST-SCHUMPETERIAN WORLD

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"It may turn out I suppose, that vested interests and personal selfishness may stand in the way [of full employment]. But the main task is producing first the intellectual conviction and then intellectually to devise the means. Insufficiency of cleverness, not of goodness is the main trouble".

John Maynard Keynes  
in a letter to  
T.S. Eliot  
1945

In hindsight, it appears that the great accomplishment of the Keynesian era was that it (temporarily) transformed political economy by bureaucratizing economics and trivializing and tranquilizing political life. Indeed, if a limitless faith in the individual's capacity to reason is the essence of liberalism, then Keynes was perhaps the greatest liberal of the 20th century — a hyper rationalist who believed that "nothing is required and nothing will avail, except a little, a very little clear thinking". And, as Keynesianism's demise has left a messy and increasingly irrational political world in its wake, the cry goes out for a new Keynes, for a new technical approach which will solve the problem of stagflation and reconstruct the blissful de-politicized world which had previously been promised by Keynes.

Of course, this is chimerical — as was the Keynesian project all along. Nonetheless, the dispelling of the illusion of Keynesianism raises the compelling question of what the 'post-Keynesian' world will settle down and be. After all, the historical purpose of Keynesianism had been to provide a means whereby capitalism's tendency to depression would be contained and the increasing demands for economic democracy would be acknowledged — but in a way which would not threaten either capitalism or liberal democracy. However, it is clear that the 'business cycle' still rules the lives of capitalist nations and their citizens, while the aspirations for economic democracy have never been fully (or even substantially) validated. So, what of capitalism and liberal democracy? What are the political implications of the transformation of the Keynesian world to a post-Keynesian one?

### I

It will be recalled that capitalism and liberal democracy had been severely threatened through the Depression and war years. Despite differences between them, the two major economic theories of the day (Classical and Marxist) agreed that the twentieth century demand by the working class for democratic access to

the fruits of economic activity was the quintessence of the Depression. Classical thinking suggested that union strength had perpetuated high wages in weak economic circumstances, such that potentially profitable investment opportunities were constrained. However, to reduce wages would require the curbing of trade union power, inevitably necessitating measures of coercion, thereby accelerating the 1930's trend to extremism and fascism. Marxists saw the Depression as resulting from labour's increasing strength in the class struggle. But to reduce economic instability via public works or increased state involvement in the economy would increase the size and control of the public sector, and place conflicting pressures on liberal democratic politics. While the war eliminated the problem of unemployment, the economic accomplishments of these years legitimized state planning, thereby inhibiting a return to the classical, laissez-faire world; on the other hand, to perpetuate the wartime approach to economic matters would be to continue a condition of political control incompatible with capitalism and traditional liberal democratic politics.

The fundamental question was whether capitalism could meet the requirements of an increasingly democratic society. It appeared that it was incapable of being stabilized unless trade union strength was curbed or unless an increased state involvement in the economy was instituted. While the latter might have doomed capitalism, both approaches raised serious doubts about the future of liberal democratic politics. Indeed, the predominant bourgeois vision of modern society in the pre-war and wartime years was a pessimistic one, a vision uncertain about the capacity of capitalism and liberal democracy to withstand the potentially destructive forces of economic instability and socio-economic demands. It was in this historical and existential context that Schumpeter confronted the question of the survival of democratic politics. In *Capitalism, Socialism and Democracy*, he concluded that there were three major pre-conditions for the existence of democratic planning of the economy: (1) the limitation of the area of political decision-making; (2) the exercise of political self-restraint both within Parliament and in society-at-large; (3) the existence of capable political leadership and a well-trained bureaucracy. These conditions were seen to be necessary if the legitimacy of the democratic process were to be sustained. Strict boundaries for political activity were needed to ensure that democratic politics would be effective within these bounds. Expectations had to be checked — both within Parliament and in society-at-large — in order that democratic politics not be swamped by potentially unrealizable demands. These conditions in turn were needed to insulate the technical experts in the bureaucracy from political pressures, to allow them to manage the economy successfully. If the economic goods were delivered, the effectiveness and legitimacy of capitalism and liberal democracy would be sustained.

What distinguished Keynesianism as an approach to economic affairs from other types of approaches was that it offered to stabilize economic conditions and respond to demands for social and economic democracy while fulfilling these Schumpeterian conditions. There is, admittedly, considerable controversy about what Keynes himself suggested in terms of analysis and policies, as well

as about which subsequent adaptations of his ideas most accurately reflects a 'Keynesian' position. It is not possible here to scrutinize Keynes's texts or to evaluate the applications of his ideas. But it is worth noting, as Schumpeter pointed out, that Keynes tended to cover his analytical tracks by attacking as well as defending classical precepts. Moreover, given the pragmatic aim of Keynes's work (directed to solving Britain's economic problems) there can be difficulties in establishing transcendental characteristics in his writings. Further, Keynes has been 'used' by a wide and eclectic array of economic theorists, policy-makers, and political groups and politicians. The result has been that 'Keynesianism' has become a generic term, its specific meaning being determined by those who have appropriated Keynes's ideas and the manner in which these ideas have been (ab)used.

As a result of these factors, it is not surprising that there are a multitude of competing versions of Keynesianism, stretching from right to left on the political continuum. But, what is critical is to note that these versions differ in the degree to which they are in tune with the Schumpeterian conditions. In order to clarify this point, four (admittedly soft) models or versions of Keynesianism are illustrated below in ideal type form.

mood/vision	Supply Side	Demand Side
PESSIMISTIC	<b>ANALYSIS:</b> Chronic Instability of investment process exacerbated by drying out of opportunities – stationary state inevitable.	<b>ANALYSIS:</b> mass poverty radically constrains production possibilities.
	<b>POLICY:</b> extensive state role in socializing investment and directing resources.	<b>POLICY:</b> state to initiate far-reaching re-distribution of resources and income to buoy production.
OPTIMISTIC	<b>ANALYSIS:</b> creative capacity of private investment constrained by economic instability and falling profits.	<b>ANALYSIS:</b> cyclical downturns exacerbated by the falling demand accompanying rising unemployment
	<b>POLICY:</b> marginal state role in keeping business confidence high; indirect incentives: subsidies, credit, countercyclical policies, etc.	<b>POLICY:</b> marginal state role in ensuring effective demand: tax changes, self-financing social security, etc.

FIGURE 1

One can categorize different variants of Keynesianism in two general ways: in terms of the 'vision' and the 'mood' of economic circumstances held by the advocates of a particular variant. In broad terms, a 'supply side' vision of Keynesianism competes with a 'demand side' one, and each has an optimistic and pessimistic variant. Each of the four resulting versions of Keynesianism presents a particular analysis of economic circumstances and a specific scenario of the role which the state should play in economic life.

Different advocates of Keynesianism found capitalism's economic instability to lie on either the supply or demand side of the basic economic equation. That is, that capitalism was prone to periodic crises was seen either as due to the absence of the proper conditions for production or as a problem of realization. The demand side vision is that most popularly associated with Keynesianism. In this view, an adequate capacity for production is seen to be constrained by the low level of demand associated with the narrow income base of the mass of the population. On the other hand, the supply side vision suggested that economic crises arose because of the fact that capitalism suffered from a chronic instability in the investment process (i.e. the process by which commodities are supplied).

The implications of each of these visions is determined by the mood of its adherents. The pessimistic supply side vision was a stagnationist one, presenting a picture of the drying out of profitable investment opportunities, the decline of capitalist spirit and enterprise, and the inevitable arrival of the stationary state. On the other hand, the more optimistic supply side adherents emphasize the continuing creative capacity and potential of private investment, which needs only encouragement and an environment conducive to private economic activity (in this way, George Gilder has contended that Keynes was a supply sider). On the demand side, pessimists concluded that the relative poverty of the population ensured that capitalism's immense productive capacities could never be fully exploited and that capitalism would continually be buffeted by crises of realization. Optimists in turn suggested that 'normal' cyclical developments in the economy were exacerbated by the falling demand associated with rising unemployment.

These distinctions take on operative significance in the way in which they form a matrix of suggested policy responses to capitalist instability. And, within this matrix, policy responses varied in the degree to which they fulfilled the Schumpeterian conditions. The pessimistic variants of Keynesianism appeared to require extensive, controlling roles for the State in the economy, which would be unlikely to fulfill the Schumpeterian conditions. On the supply side, the State would have to do the job which capitalists appeared to be unable and/or unwilling to do. This would require the socialization of supply side activity and state directing of investment and economic resources. On the demand side, the State would have to act to socialize consumption through a fundamental and politically tricky redistribution of economic wealth and resources, in order to ensure an adequate level of effective demand. The more optimistic variants appeared to require a far less dramatic role for the State, which would be more likely to fulfill the Schumpeterian conditions. Optimism on the supply side implied but a marginal and indirect role for the State in producing a "proper economic environment" which would ensure business confidence and healthy levels of investment in a continued free enterprise world. This 'environmental' role suggested a policy agenda which would include low taxes, cheap credit, subsidies, etc., as well as countercyclical budgeting and policies to ensure buoyant demand, which would act as an inducement to investment and the

supply side. Depending on the degree of optimism within the demand side vision, the redistribution necessary to ensure adequate levels of demand might only be marginal in degree or take place episodically. This could easily be accomplished through tinkering with the tax system and/or by establishing self-financing social welfare programmes.

Governments and political leaders had their own visions of particular economic and political circumstances to which they had to respond, and they chose that version (or combination of versions) of Keynesianism which appeared to them to be the most appropriate and politically expedient. Countries with serious problems, statist traditions, and/or weak capitalist ideology tended to opt for the more interventionist variants, with the degree of seriousness of legitimacy and accumulation problems determining the supply or demand emphasis. Those countries with the greatest 'liberal parliamentary sensibilities' (arguably, the Anglo-American democracies) tended to embrace the less interventionist versions of Keynesianism, as these were more readily amenable to fulfilling the conditions for perpetuating liberal democratic politics. In turn, they tended to balance legitimacy and accumulation needs by mixing supply and demand policies.

In this paper, Keynesianism refers to this second tendency, to the political approach to socio-economic matters which was most alive to the Schumpeterian requirements for the perpetuation of liberal democratic politics. This version comprises mainly the optimistic and supply side variants, and will be termed supply-side Keynesianism. It may appear to be perverse to use this phrase, given Keynes's rejection of Say's Law (viz. supply creating its own demand) and his focus on effective demand producing employment. But, supply side Keynesianism has been used as a phrase to emphasize that, in the last analysis, private activity in a free market economy would continue to determine the basic allocation and distribution of resources. Indeed, this Keynesian argument has been that, once governments acted to produce the 'proper environment' (including a sufficient level of demand), then supply conditions and the market would look after themselves and generate a high degree of economic activity and employment. Governments would simply keep a close eye on economic circumstances, taking action to encourage private economic activity whenever a cyclical downturn threatened. Then, indirect or 'environmental' actions could be initiated, including countercyclical budgeting, low interest rates, subsidies, as well as economic and social security measures. But, governments did not have to be concerned about controlling the economic terrain, or shaping the specifics of what was demanded, the details of investment decisions or the kinds of employment produced. Governments would only produce generalized macro inducements, while the market would continue to determine the specific patterns of allocation and distribution. And, as governments would be reacting to marginal and short-term fluctuations in the economy, their involvement would be episodic and incremental, not permanent and ambitious.

Relative to earlier expectations about what would be needed to stabilize capitalism and absorb demands for social and economic democracy, this

approach was politically restrained, and emphasized that — as long as the proper economic environment was perpetuated — private economic activity and the supply side had the capacity to generate employment and economic stability. This supply-side, market-oriented version of Keynesianism differs dramatically from that planning-oriented version which rests on Keynes's famous phrase in the *General Theory* that "a somewhat comprehensive socialization of investment will prove to be the only means of securing an approximation to full employment". Adherents of a more interventionist Keynesianism have thus argued that political control of investment decisions would be needed, as well as the elimination of private rights to the allocation of resources and the initiation of long-term comprehensive planning. There has been considerable confusion about this point. One can certainly make the case — from the supply-side perspective — that chronic instability in the private investment process must be countered by a greater degree of socialization of the allocation of resources. But, this would widen the politico-economic agenda, increase political expectations about economic matters, and ensure that politics and economics would be integrated and not insulated from each other; that is, the Schumpeterian conditions would no longer be fulfilled. On the other hand, it also can be maintained — in supply-side, market-oriented terms — that Keynes was not referring to political control of investment decisions but rather to the *overall level* of investment which was needed to ensure the full use of economic resources. "... apart from the necessity of central controls to bring about an adjustment between the propensity to consume and the inducement to invest, there is no more reason to socialize economic life than before ... I see no reason to suppose that the existing system seriously misemploys the factors of production which are in use ... when 9,000,000 are employed out of 10,000,000 willing and able to work, there is no evidence to suggest that the 9,000,000 men ought to be employed on different tasks, but that tasks should be available for the remaining 1,000,000 men. It is in determining the volume, not the direction, of actual employment that the existing system has broken down". After defending the classical view of things in this regard, Keynes then proceeded to a vigorous defence of the virtues of the capitalist market system, praising the advantages of efficiency, decentralization, individual freedom and initiative which it allowed. Here, then, is the way in which George Gilder can see Keynes as a "supply-sider", for this is the manner in which this particular version of Keynesianism was committed to the continuation of capitalism and the perpetuation of liberal democratic politics.

The supply-side, market-oriented variant of Keynesianism offered to fulfill the three Schumpeterian conditions for liberal democracy. First, it contributed to the establishment of strict and limited boundaries for the exercise of democratic politics and the perpetuation of the authority of the market. Controversial (and threatening) matters relating to distribution and ownership were removed from the political agenda by Keynesianism's focus on the elimination of unemployment via limited economic management. By perpetuating the market system, specific, detailed and micro decisions were to be

made by individuals in the market and not in the political arena. Generalized and limited Keynesian policies presented a far less involved and less divisive political agenda than socialized investment, economic plans, and National Policies would have produced. These latter actions would have required a considerable degree of consensus building which, in turn, would have required a particular array of social forces in the community. If this was lacking, these policies would either fail or quickly become illegitimate, bringing tremendous pressure to bear on liberal democratic politics. Instead, the limited range of decisions on the policy agenda and the minimization of the difficulties of consensus building ensured that pressures on liberal democratic politics would be minimized.

Second, these pressures were also limited by this Keynesian project's apparent capacity to generate political self-restraint. On the one hand, the very promise of a limited agenda and a relatively passive role for government was a promise which deflected considerable private expectations to the market place. This was particularly the case for labour. The promise of the socialization of uncertainty (via counter-cyclical policies and a modicum of social security) was traded on to the political agenda in return for the withdrawal from the agenda of fundamental questions about ownership, distribution and political control of the economy. This placed severe limits both on public expectations of what democratic politics would do in the economy as well as on what politicians would be allowed to do. This commanded the attention of politicians themselves, as they were presented with the possibility of stabilizing economic conditions and responding to working class demands, but without introducing radical programmes, nationalization, controls, etc. — any of which could have alienated considerable political support. On the other hand, Keynesian policy provisions promised to be of a generalized, macro sort, which would not display specific costs and benefits but rather universal advantages. This set a political framework in which the ostensible neutrality of policies would inhibit the escalation of political demands in response to perceptions of political favoritism. For labour and the political left, full employment was offered, as well as economic stability, social security, an increased role for the state, and a validation of working class claims for economic democracy (viz. increasing labour income sustaining national income and economic stability). For capitalists and the political right, the rejection of public ownership and state planning was appealing, as was the Keynesian vision of a market-based economic stability, encouraged through a policy of low taxation and interest rates. For the middle class and the political centre, there was the promise of economic and political stability, with no drastic increase in taxation, and a common sense, pragmatic state orientation to a vibrant market economy. That policies would be "in the interests of all" eased anxiety about an active government favouring one group over another. This eased expectations and pressures about what democratic politics would do in the economy. Moreover, what had previously been a politicized and ideological context for economic matters was defused by the vision of a benign government, aided by its expert

bureaucracy, rationally, routinely and technically managing the economy; all of this seemed 'beyond politics' and more akin to the world of accounting.

Third, this Keynesianism promised to continue to centralize power, at the centre, away from the margins, at the executive level away from the legislature, and to the experts away from the amateur politician. The Keynesian accomplishment of limiting the range of politics and generating self-restraint was critical, for it allowed the technical, bureaucratic realm to remain insulated from politics. The extension of the 'bureaucratization of politics' and the triumph of the authority of technique ensured that 'irrational' sectoral and political intrusion or unrealizable demands would not undermine the capacity of the technical realm to manage the economy effectively. As long as 'apolitical', 'technical' and 'pragmatic' policy delivered the goods, the public would be happy, and the perception of the effectiveness and legitimacy of liberal democratic politics would be sustained.

In sum, this version of Keynesianism offered the prospects of a stabilized capitalism, acknowledgment of demands for social and economic security, and the fulfilling of the Schumpeterian conditions for liberal democratic politics. The market would be left to get on with the job of allocating economic resources and rewards, thereby allowing liberal democratic politics to avoid agonizing and divisive choices about economic matters.

## II

The supply-side market-oriented variant of Keynesianism offered the possibility of a particular style of politics and a distinctive approach to economic policy. As bureaucratic management delivered the economic goods, expectations would be realized and social pressures on governments would be eased. And, as Keynesian policies were limited and seen to be in the interests of all, the legitimacy of governments' actions could be assumed and their apolitical qualities be trumpeted. This scenario was promised as a result of an analysis which suggested that economic prosperity could be maintained through the initiation of a limited array of generalized demand policies (as opposed to an extensive array of detailed supply and planning policies). Hence, it was anticipated that Keynesian politics would comprise a constrained world, involving but the routine application of rationality and technique. And, this 'democratic elitist', Schumpeterian world more or less unfolded as anticipated. The bureaucratization of economic affairs produced the bland, tranquilized 1950s, while a limited welfare system and a more developed system of consumer credit generated the mass gratification of the consumer society of the 1960s. All the while, politics was distinguished by its paternalistic style, low levels of participation and the routinized application of technique to social problems. In short, it appeared that the successes of Keynesianism had accomplished the elimination of class politics, the end of ideology and the coming of the post-industrial society.



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More nuancé analysis than is possible here would demonstrate that this picture is somewhat overdrawn and inaccurate. While it is impossible here to catalogue what actually happened in the post-war period, Irwin Gillespie — and others — have indicated that the extent of application of Keynesian policy was very limited (*Canadian Tax Journal*, May-June 1979), and economic stability and full employment were never realized. On innumerable occasions, governments did not anticipate or mitigate economic problems and did not pursue policies in tune with this particular version of Keynesianism. Over the years, successive governments adopted other types of tools and policy objectives (balanced budgeting, sectoral planning, etc.) such that supply-side, market-oriented Keynesianism was relegated to a secondary if not a marginal position. From early in the post-war period through to the late 1960's, the view emerged and persisted that this Keynesian approach could not deal effectively with a variety of crucial economic factors and situations. Indeed, any reasonable expectation as to the possible concretization of this Keynesian vision had withered away by the late 1960's.

If this is the case, whence the view that post-war economic and social stability was largely due to the successful use of Keynesian policy? The adoption and ostensibly successful perpetuation of this Keynesian approach was a function of three broad factors. First, this was a period in which there was tremendous optimism about the potential social benefits of applying collective human intelligence to rational economic management. While liberals had first trumpeted the efficacy of human intelligence, the socialists had appropriated the issue and reconstructed it into a notion of collective intelligence which, it was anticipated, would be expressed through the plan. Liberals had traditionally advocated laissez-faire in the economic realm, contending that not only did individuals best know their own self-interest, but that they were capable and intelligent enough to realize it. But, as Keynes and other liberals saw, the world — if left to run itself — would not always generate benign results: "The world is not so governed from above that private and social interests always coincide". So, liberals extended their rationalist faith from the individual to the social group (viz. the bureaucracy), without their optimistic rationalism weakening: "Experience does not show that individuals, when they make up a social unit, are always less clear-sighted than when they act separately". This orientation was bolstered substantially by the successful planning experience of World War II, which had established the new authority of technique. Indeed, there was considerable bureaucratic and political consensus by war's end as to the nature and direction of economic policy. As a result, there was persistent faith in the post-war period that the rational application of Keynesian techniques would ensure stable economic circumstances. This optimistic rationalism in turn contributed to the continued authority of the market. Despite the broad criticisms lodged against capitalism during the 1930s and early 1940s, capitalism entered and survived the postwar period with a surprising degree of legitimacy. This was the result of the widespread confidence that Keynesianism's limited intervention in the economy would ensure that the market would generate economic growth and stability.

Hence, the postwar period was dominated by the twin authorities of technique and the market, contributing to the illusion that successful Keynesian management was responsible for the economic prosperity of these years. This dominance was bolstered by two other critical factors of this period. Whatever its motives, American leadership of the postwar Bretton Woods system resulted in two decades of relatively stable international economic conditions and substantial consensus amongst the Western industrialized nations. After World War II, the United States was willing and able to establish a 'managed' international economic system, a system based on the principle of free movement of capital, goods and exchange, but one effectively managed by the United States through the dollar as the accepted international unit of exchange. While the Americans benefitted immeasurably from this 'liberal imperial' system (by printing dollars it financed its military and political expenses and expanded its multinational corporations throughout the world), its allies accepted the system, given the liquidity generated and the economic and political stability which was created. The reign of the American dollar encouraged a rapid expansion of trade and international economic activity from which all countries — Canada included — benefitted immensely. This in turn contributed substantially to sustaining the authority of the market and Keynesian technique, as did the third factor, the unfolding of the long-term postwar boom. Despite prophecies of imminent collapse, the international capitalist system generated substantial growth in the post-war period. Given a variety of technological developments (electronics, transportation and communication, chemicals, etc.), cheap energy, a large and relatively quiescent labour force, stable international economic conditions and market-oriented governments, there was substantial business confidence and extensive opportunities for profitable private economic activity. This tendency was strengthened by the evolution of the Cold War, which created immense demand for raw materials, armaments and high technology equipment. Given the prospect of economic stability and full employment (as well as social security) relations between capital and labour were more or less stabilized, and social and ideological pressures on governments were restrained.

Thus, optimistic rationalism, the protective umbrella of American empire and the long-term boom contributed to the persistence of the illusion that it was the exercise of Keynesian analysis and policy which had produced perpetual economic stability and prosperity. This was the context in which the pessimistic, stagnationist version of Keynesianism could be rejected in favour of the more optimistic supply-side, market-oriented version. However, with the passing of these three conditions, the authority of Keynesian technique was undermined. First, the hyper-rationalism of Keynesianism created overoptimistic anticipation about the capacity of the Keynesian design to accurately analyse economic conditions and initiate appropriate and successful policies. Governments formulated policies on the basis of limited information and constrained knowledge — given the continued predominance of the market. Not only were governments perpetually uncertain about market conditions and private

intentions, there was no certainty that individuals in the market would react to governments' inducements in the desired manner. Similarly, there were elements of the market economy which could not be influenced through the use of Keynesian policy. It also became apparent that micro and supply factors and the long run pattern of economic development affected the possibility of attaining high levels of employment and economic stability, and the Keynesian design could not address these possibilities. Hence, a variety of economic problems existed (even during the most apparently stable economic circumstances), including regional, sectoral, structural and international problems. But, it was the development and persistence of inflation which weakened the authority of technique and undermined the confidence that the economy could be managed effectively. Given a variety of technical constraints, the existence of market power, the basic asymmetry of its design and competing policy objectives, the Keynesian design was singularly ill-suited to cope with inflation. Symbolically, perhaps, the Keynesian era ended with Milton Friedman's Presidential Address to the American Economic Association in 1967. In attacking the idea of the Phillips curve (which had ostensibly demonstrated a trade-off between unemployment and inflation), Friedman and his monetarist followers weakened the optimism and consensus that the Keynesian tools could be used to promote economic stability. Further, they also challenged the rationalists' contention that collective human intelligence could be used to manage the economy. Moreover, the persistence of regional, sectoral, structural and international problems and — particularly — the simultaneous existence of unemployment and inflation signified that the market was not functioning properly. In general, as the perception arose that economic policy was ineffective, the authority of technique declined; as the perception grew that the market was not functioning, the authority of the market was diminished.

The weakening of the post-war's optimistic rationalism was a function of the degeneration of the economic circumstances which had sustained the twin authorities of the market and of technique through the postwar period. By the late 1960's, the United States had become unable to provide the international political leadership necessary to stabilize the international economy; indeed, by 1971, the Bretton Woods system had unravelled. From the Canadian perspective, there were two important consequences. First, by exploiting their dollar authority, the Americans had sustained their political, military and economic predominance internationally. This was particularly the case during the Vietnam War. As the Americans acted to retain their military authority, the expenses of the war conflicted with the expenses associated with the effort to retain legitimacy domestically; rather than choosing one over the other, increasingly worthless and non-redeemable dollars were used to finance both objectives. This generated considerable inflationary pressures from which the Canadian economy could not hide, given the continued predominance of the open market and the intimacy of the Canadian-American economic relationship. Second, as the regenerated European and Japanese nations began to reconsider the costs of American military and political leadership, tensions arose within the

western alliance. Further, as the Europeans and Japanese came to outcompete the United States, and as the costs of military and political empire accumulated, the American balance of payments situation deteriorated seriously. In order to protect itself, the United States imposed trade and investment controls and made the dollar inconvertible. These controls seriously affected the Canadian economy and constrained the formulation of its economic policy. In general, given the rise in international economic competitiveness (and the development of regional trading blocs), and given the uncertainty in world political and economic conditions, Canada began to lose the benefits of a stable international economic system. As a result, the authority of Keynesian techniques was weakened, as these were developments and problems to which the Keynesian design could not address itself.

The results of the degeneration of the conditions of long-term growth were similar. Growth had previously insulated economic management from political and ideological pressures and conflicts. The quiescence of the labour force, the confidence and activism of capitalists, and the consensus or accommodation between capital and labour had been generated and nourished by sustained economic growth. As the long-term boom came to a close, groups and classes scrambled to protect their economic interests. Governments were unable to control this development, unless they made fundamental decisions on economic distribution. Unwilling and/or unable to do this, inflation developed as a surrogate for economic growth in governments' attempts to deal with continued expectations of economic prosperity. However, as inflation persisted and intensified, the authority of technique and of the market was further undermined (particularly as there was uneven success in self-protective measures). Hence, inflation destroyed the barriers which had insulated economics from politics and generated political and ideological pressures on governments, pressures to which Keynesianism could not respond.

With the decline in the authority of Keynesian rationalism and technique, the weakening of the post-war boom and the destabilizing of the world economy, the illusion of the capacity of the supply-side, market-oriented Keynesian design was dispelled and the possibility of Keynesianism politics was undermined. Given the persistence of the idea of government responsibility for economic circumstances, there was ever-increasing pressures placed on governments to redress economic problems whenever bureaucratic management did not deliver the goods in a satisfactory manner. But, as public expectations about governments' actions increased, the politico-economic agenda widened to include a range of non-Keynesian issues and objectives. As a result, there was decreasing opportunity for the Schumpeterian conditions to be fulfilled.

First, to the extent that governments moved from the passive, 'environmental' Keynesian role to a more active interventionist one, they also moved from the realm of 'apolitical' policy back to the political world of tensions and controversies about economic matters. Once governments introduced sectoral and planning measures ("disaggregated" policies), these policies became far

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more detailed and specific than generalized Keynesian measures, and involved far more specific and obvious costs and benefits. The more detailed and specific governments' policies became, the harder it was for them to portray their actions as being neutral or in the interests of all. Hence, it could no longer be assumed that governments' actions would be accepted as being legitimate. Similarly, as political involvement in the economy increased, governments became open to the charge of spawning an unmanageable bureaucracy and of infringing on business and property rights. Supply-side, market-oriented Keynesianism had promised to avoid precisely these sorts of problems, by limiting the range of the policy agenda and minimizing the difficulties of consensus-building. But, the transition to a more interventionist role resulted in governments confronting a variety of conflicts over economic policy decisions, and a diminished possibility for constructing a consensus around their policies.

Second, the bureaucracy faced increasingly formidable technical problems in the form of more complicated economic analysis and more nuance policy, as a result of increased state intervention in the economy. The more complex that analysis and policy became, the less likely it was that the bureaucracy would be successful in delivering the economic goods. In conjunction with the evolution of a contradictory police agenda (viz. increased and conflicting social pressures and expectations), this led to a decline in the likelihood of the effectiveness of government action in the economy. Ultimately, this decline in effectiveness (or at least the perception of ineffectiveness) resulted in the collapse of the legitimacy of governments' actions.

So, with the demise of the Keynesian era, the Schumpeterian conditions for liberal democratic politics were severely weakened. In conjunction with stagnationist concerns about the future of capitalism, Schumpeterian concerns arose that overextended expectations and overloaded government threatened liberal democratic politics. A widening politico-economic agenda and persistent expectations ensured that the bureaucracy and the market could not be insulated from political and ideological pressures. Hence, there was a concern that liberal democratic governments could not long sustain their legitimacy under conditions in which they appeared to be perpetually ineffective.

### III

Once the Keynesian illusion had been dissipated, governments were confronted by two broad policy options with respect to troubled economic circumstances, neither of which appeared to have the capacity to reconstruct the Schumpeterian conditions. First, in reaction to the severe weakening of the forces of economic growth and the 'muddled failures' of an incremental, market-oriented Keynesian approach, governments could seriously extend their presence in the economy to stimulate economic growth and shape the market and economic development to a desired, non-inflationary pattern. Government measures would include economic controls (of wages, prices and profits), long-term industrial strategies (to ensure the 'best' allocation of resources as well as

international competitiveness), and increased emphasis on re-distributive and equity goals. Rejecting the claims that social expectations were not valid, the planning approach argues that governments' failures to realize these expectations were the result of the formulation of half-hearted policies which continued to rely on market forces. Hence, it was expected that with a 'rearrangement' of economic development and a fuller application of collective human knowledge, economic circumstances could be dramatically improved and social expectations more fully realized. And, governments in Canada took tentative steps in this direction throughout the 1970's and early 1980's, in the form of wage and price controls and industrial development programmes. Nonetheless, the post-controls economic orientation of the government ('The Way Ahead') was distinctly market-oriented (despite Trudeau's New Year's Eve Galbraithian ruminations about the 'new society'). Similarly, while governments were willing to speculate about the industrial strategy needed to pump-up economic growth in Canada, Richard French ('How Ottawa Decides') has shown how the formulation of this strategy over the last decade and longer has been marked by tensions between planning and market principles; the Finance Department's market orientation has persistently emerged triumphant over the planning proposals of the Industrial Departments, such that Canada entered the 1980's with an industrial 'strategy' which remained an essentially market-oriented one (Olson and Johnston's private sector-based plans).

The on-again, off-again Canadian flirtation with planning — a running theme of post-war Canadian life from World War II through the Diefenbaker years, the Economic Council of Canada, the CDC, etc. — reflects a continued ambivalence about the role of the state in the economy. Planning proposals and actions generate serious political controversy, reflecting concerns about the propriety of state control of the economy as well as Schumpeterian anxiety about its impact on political democracy. These controversies and inhibitions have reflected three considerations surrounding the planning orientation, all of which have constrained the reconstruction of the Schumpeterian conditions. First, there is serious concern about whether the actual planning policies adopted will be successful in realizing the objectives of this approach. The planning orientation attempts to extend the post war's optimistic rationalism that collective knowledge can be used to improve the economic situation. However, given what appeared to be the perpetual failures of economic policies in the late 1960's and 1970's, there is far less confidence in the early 1980's that far-reaching and ambitious economic programmes would be successful. As noted earlier, the more ambitious the policy which is designed, the greater the likelihood that it will be ill-conceived and/or founded upon incorrect analysis of economic circumstances. And, a failed ambitious policy would generate serious economic damages leaving the political initiators of the policy in a severely weakened political situation. Indeed, the Canadian government's economic and fiscal strategy for the 1980's — centred on accelerated resource development with spin-off industrial developments — foundered on the unanticipated collapse of the world market and resource prices. The bits and pieces of this

particular strategy are still being collected as major industrial projects stall, private investment stagnates, unemployment rushes to two million and the legitimacy of the government plummets. While Keynesianism had offered minimal political risks and potentially high political benefits, planning policies offer huge political risks and costs, particularly as the potential benefits of these policies are long-term in arriving while political expectations are fundamentally short term in nature. In short, the post-Keynesian era is marked by a pessimism that there are 'rational solutions' to economic problems waiting to be discovered and supplied by governments and their bureaucracies. As a result, there is considerable wariness about the economic and political risks of the planning orientation.

Second, even if it could be contended that a rational solution to economic problems existed, there continues to be an absence of a viable ideological or moral orientation in Canada that could be used by governments to guide them in their policy decisions. There is simply no consensus in Canada about what these plans and policies should be. The Keynesian approach had anticipated no difficulties in this regard (as a result of its limited policy agenda and its promise of non-discriminatory and universal benefits). However, the planning orientation cannot assume the existence of a consensus around any particular matrix of policy decisions, given the greater ambitiousness of its agenda and of its programmes and the fact that these decisions would produce more obvious and specific winners and losers in the economy (regionally, sectorally, etc.). Whenever governments introduce planning devices or policies, or intervene in a specific or detailed way, they have great difficulty in portraying their actions as being in the national or collective interest. As a result, policies emanating from the planning orientation have tended to exacerbate regional and sectoral tensions in Canada, and perpetuated the context of a beleaguered and illegitimate government, doing battle with society. In short, the post-Keynesian era requires a new ideological framework or consensus for economic policies, the absence of which will ensure that policy decisions will generate substantial political conflict and controversy.

Third, there is considerable doubt about whether the planning option can be pursued in liberal democratic fashion and fulfill the Schumpeterian conditions. The planning option widens the politico-economic agenda, raises expectations about the capacity of governments' actions and makes economic matters an exclusively political responsibility — in short, it burdens liberal democratic politics with crushing pressures. Given the absence of any obvious consensus-building formula, given the likelihood of policy failures, and given rapid technological change and a highly competitive world, could liberal democratic policies survive these pressures? To carry out the planning option, governments would have to negate the impact of market processes, and deal with international forces, foreign ownership, large corporations and unions, and technological changes. Only in this way could planning policies become operative or have any chance of success. Similarly, any 'new national policy' in Canada would probably require centralization of political power and the imposition of the

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policy on to the provinces, given present political divisiveness. There is profound political anxiety that illiberal measures would be required to overcome the constitutional, international and socio-economic roadblocks which stand in the path of the planning option. All of this is in stark contrast to the Schumpeterian promises of the supply-side, market oriented variant of Keynesianism, which had promised a constrained political world in which stresses and strains on liberal democratic politics would be minimal.

Hence, governments' flirtation with the planning orientation has been inhibited by the decline in optimistic rationalism, the absence of ideological and economic consensus, and the fear of political authoritarianism. And, these factors have been the stuff out of which the second post-Keynesian policy option was constructed, that is, the market orientation. As a result of the perception of the ineffectiveness of governments' economic policies as well as because of the political tensions generated by increased state participation in the economy, governments' actions in the economy from the late 1960's onward experienced diminishing legitimacy. It is in this context that proponents of the market orientation suggest that governments should radically retrench their role in the economy. Given the limits to collective knowledge and policy rationality, it is argued that planning or pseudo-planning approaches should be resisted, as economic processes and developments are simply too complex for politicians and bureaucrats to understand. Indeed, the last decade's decline in productivity and economic growth is seen to have been a function of irrational bureaucratic and political interference which has resulted in the protection of inefficient enterprises and the squeezing out by governments of private activity in the market. As the rate of growth began to decline, political action to avoid a recession is seen to have perpetuated high wages and prices, ballooning government spending and deficits, and a frantic increase in the money supply, all of which generated inflation and a further deterioration of economic rationality. Hence, a treadmill of declining growth, partial response, inflation, declining productivity, etc. With respect to the political realm, it is argued that politicians purchase electoral votes through the abuse of their budgetary resources; not only did this squeeze out private market activity (as government spending and deficits shifted resources to the private sector), but this process created 'over-extended' social expectations, which legitimized misleading and dangerous notions about equity, equality and the capacity of political action to improve economic circumstances. In general, advocates of the market orientation contend that the market has been overheated by excess demands while the political process has been made volatile as a result of an 'overloaded' agenda and perpetual political and ideological squabbling about economic matters.

Hence, advocates of the second option are sympathetic to the Schumpeterian concerns about democratic politics and militate for a radical retrenchment of the state's role in economic life. On the one hand, it is contended that if the market is 'freed' and cleansed of its political and ideological impurities, then economic rationality will be reconstructed, growth and productivity will rise, and there will be decreased pressures for government action in the economy.



Inefficient firms will improve themselves or go bust; artificially high wages or prices will be penalized by bankruptcies and unemployment. In short, responsibility for economic matters should be returned to the market, which will generate a more rational realignment of economic resources than politicians and bureaucracies could hope to attain. Similarly, it is contended by the market advocates that once economic matters are removed from the political agenda, then political, ideological and class pressures will be released from the democratic process and returned to the market place. Expectations about governments' economic actions will hopefully decline, and controversies about economic distribution and the allocation of resources will be worked out via the benevolent oppression of the market process. It is anticipated that this will rekindle the initiative and enterprise of more self-reliant individuals and industries, leading to a renaissance of market activity.

This option was embraced to an extent in Canada, in the form of the monetarist economic policies of the late 1970's and early 1980's, as well as in the attempts by governments to limit spending, repair the budgetary imbalance, promote private investment and deflate public expectations. Moreover, as noted earlier, industrial strategies have had a distinct market-orientation. However, as with respect to the first option, governments have remained ambivalent about the extent to which they should shed their post-war political responsibilities and allow market forces exclusively to determine economic outcomes. The result, then, has been an on-again, off-again flirtation with monetarism and supply-side strategies. While social security programmes have been threatened, governments have not ravaged them, with the result that most Canadians remain 'corrupted' by their relationship with the state. Moreover, while unemployment has been high and rising, corporations threatened with bankruptcy have received substantial government assistance and the government itself continues to intervene in the economy. This reticence to cast Canada's economic fate to the winds of the market place reflects two broad considerations, which also constrain the reconstruction of the Schumpeterian conditions.

First, as with respect to the planning option, there are serious doubts about whether the policies of the market orientation will realize their objectives. While the planning option remains faithful to the optimistic rationalism of the post-war era, the market orientation is an energetic expression of the faith in the market's capacity to produce an effective and acceptable matrix of economic outcomes. However, governments and observers have had doubts about whether a 'freed' market economy would regenerate itself, producing born-again capitalists and soaring investment and productivity levels. Recent experience in the U.K., U.S.A. and Canada has indicated that market-oriented policies have been less successful than anticipated: supply side inducements have not led to a flood of private investment while the techniques of monetary controls have proved to be both too difficult and unsuccessful. As in the planning option, the market approach holds serious political risks. The potential beneficial results of marked regeneration will be medium-to-long term in arriving; however, political expectations are short-term in nature, and will confront rising unemployment

and bankruptcies. In short, the post-Keynesian era has recently been marked by a pessimism that the market has the capacity to sort out the pressing economic problems of the late 20th century. As a result, governments remain sufficiently wary of the economic and political risks to shy away from a full embracing of the market option.

Second, it is unclear whether social expectations about economic and social security and government involvement in the economy can be dramatically altered without resorting to illiberal political measures. The market approach demands the diminishing of expectations, but these expectations and government responsibility for them have been continuously validated over two generations. Cutting government spending, eliminating social and economic programmes, and deliberately generating unemployment and bankruptcies raises intense political questions of equity and social morality which can be answered only by referring to the ideology of free market capitalism. But, it is extremely doubtful whether a mass commitment to a market morality can be reaffirmed. Moreover, this morality is only weakly embraced by those most dominant in the market place; large corporations — with the assistance of government — have planned and carried out extensive economic programmes, shaping markets in the process. Some of them are sluggish and inefficient and will have to go, once the market approach is initiated. But, it is inconceivable that they will go bankrupt or be taken over while placing less negative pressures on governments than that placed by the mass of the population affected by these policies. In the absence of an economic and ideological consensus around a market approach, it will be difficult for governments to portray these market measures as being in the interests of all. In short, while expectations will certainly be assaulted by initiating these measures, it is unlikely that expectations could be sufficiently diminished without the stimulus of draconian political action. While ideological and class pressures may be directed to the market place, the 'benevolent oppression' of the market place may not be forceful enough to resolve these conflicts. Given the recent weakening of faith in the powers of the market process, and the absence of an ideological consensus around a market morality, it is inconceivable that an exclusively market approach could be pursued successfully without resort to illiberal measures and political coercion.

Thus, it is apparent that the post-Keynesian world is markedly different than the Keynesian one promised to be. While there was considerable optimism about Keynesianism's capacity to deliver economic and social stability, there are now serious doubts about whether either of the post-Keynesian options will be successful or can be carried out as designed. Moreover, in contrast to the Keynesian promise to minimize political pressures on governments and ensure the continuation of liberal democratic politics, both of the post-Keynesian policy options involve considerable political risks for governments which threaten the stability of liberal democratic politics. On neither technical nor ideological grounds does there appear to be a consensus around either of the post-Keynesian alternatives. As a result, as events in the 1970's and early 1980's have demonstrated, successive governments in Canada have rejected an

exclusive reliance on either option. While governments responded to pressures to intervene in the economy to improve economic circumstances, they have been wary about the effectiveness of these policies and about the impact of these policies on the traditional Canadian liberal democratic 'way of life'. On the other hand, governments acknowledged the economic powers of the market place, but they have remained concerned that an exclusive reliance on a market orientation would not generate satisfactory economic circumstances and would lead to an unfair distribution of economic rewards and punishments. So, fearing the divisiveness which would result from embracing either approach, governments have pursued both strategies, with the result that there was little chance that their policies would be successful. And, given the continued lack of policy effectiveness, the legitimacy of governments continued to wane.

The major political implication of the demise of the Keynesian era is that neither of the post-Keynesian policy alternatives appear to be capable of reconstructing the Schumpeterian conditions. Keynesianism had appeared to resolve the problem of how the state could involve itself in the economy to ensure socially desired results in a way which did not threaten capitalism or liberal democratic politics. However, the planning and market options necessitate, yet again, fundamental choices about the role and style of politics in economic life. And, compared to these two options, the Keynesian world looks blissful indeed. And so the cry goes out for a new Keynes to come along and propose a 'technical' solution to the problems of inflation and economic stagnation.

But, this is chimerical, as was — perhaps — the Keynesian project all along. Schumpeter certainly thought that the Keynesian design was ahistorical and politically naive. And, as one attempts to sort out the character of the post-Keynesian world, one is confronted again by three Schumpeterian concerns. First, can democratic politics long survive and retain legitimacy if it continually produces policies which are perceived to be ineffective? There is considerable evidence that suggests that the capitalist system is going through a downturn of the 'long cycle'; other evidence suggests that a fundamental technological revolution is unfolding which will take a generation or longer to sort out. Whatever the case, it appears that an extended period of economic and social dislocation is about to be endured and that — optimistic rationalism put aside — there may be little that governments can do, short of initiating draconian measures. If this is the case, then governments' policies will continue to be ineffective and their legitimacy will decline. Nonetheless, pressures on governments will continue to mount to initiate non-existent solutions. How long will increasingly illegitimate governments resist the temptation/necessity to act in authoritarian fashion to impose social and economic stability?

Second, are there exhaustively rational ways of viewing our increasingly and bizarrely complex technological world? How optimistic can one be about the existence of 'rational' solutions to complex economic problems, ready to be discovered and applied by politicians and bureaucrats? Of course, the absence of rational approaches and policies exacerbates the first issue presented above. On the other hand, the experts' and governments' presentation of the rational or

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'miracle' solution may be socially unpalatable. Whither democracy in conditions in which 'technological necessities' require unpopular policies?

Third, if neither of the post-Keynesian alternatives appears to be capable of reconstructing the Schumpeterian conditions for liberal democratic politics, then perhaps it is necessary to enter into the 'post-Schumpeterian' political world. If it can no longer be assumed that political leadership and its bureaucracy can deliver the goods in rational and desired fashion, then continued ineffectiveness will lead to the decline in democratic governments' legitimacy. And, if Schumpeterian politics persist, it is inevitable that political and bureaucratic elites will move towards extreme policies and an authoritarian style of politics. Hence, the Schumpeterian vision appears to be less compelling (or even unreasonable) at present, as this particular vision of democracy may no longer offer any political attractions. Indeed, a vigorous case can be made that the post-Keynesian world requires the reconstruction of the classical democratic vision of a radical participatory democracy. On the one hand, traditional notions of 'rationality' appear to have become anachronistic in a hyper-technological environment; surely what is rational about the way economic resources are used must be determined in any increasingly social and democratic way. Only a participatory style of politics can ensure this. On the other hand, even if the economic results of this approach are no less unsatisfactory than the alternative approaches, these results stand a better chance of being accepted if the process generating these results is seen to be legitimate. Indeed, this participatory approach to public economic policy may be the only approach which can perpetuate a democratic style of politics. And, despite traditional concerns about the inefficiency and impracticality of a classical democratic approach, it is highly unlikely that it would generate any worse results than the Schumpeterian, bureaucratic approach is now presenting.

The livelihoods and future of the mass of the population is presently being affected by the daily changes of a relentless technological transformation. Past experience suggests that the (corporate-dominated) market process will not sort out these changes to benefit the mass of the population. And, as present analysis suggests there is little reason to anticipate that this process will be well-managed by the political and bureaucratic elite. Obvious political roadblocks notwithstanding, surely the time is ripe to resurrect the idea that those whose lives are most dramatically affected by these decisions should contribute to the formation of economic policy and to the construction of strategies for the use of technology and resources?

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