Competition and Welfare in Post Keynesian Economics

Prepared for Western Social Science Association 51st Annual Conference, Hyatt Regency Hotel, Albuquerque, New Mexico, USA, April 15-18, 2009-04-21

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Abstract: Whereas some Post Keynesians contend that economic power is essential for reducing uncertainty for business firms in the market, others argue that economic power of capital tends to have a negative impact on wages and unemployment, thereby creating uncertainty for working people and hence for the economy. It seems that there is a paradox: reducing uncertainty on the part of capital heightens uncertainty on the side of labor. The underlying contention in this essay is that market power, rather than solving the problem of uncertainty, fuels it by creating an unequal distribution of income, unemployment, and economic stagnation. Therefore, an activist state that takes care of the unemployed, poor, sick, and old lies at the heart of Post Keynesian economics. While the first part analyzes the linkage between competition, uncertainty, and power in the market by outlining market competition in the Post Keynesian tradition, the second section connects uncertainty to the democratic welfare state through freedom, before stating conclusions in the third section.

Some Post Keynesians contend that economic power is essential for reducing uncertainty for business enterprises in the market (Dunn: 2008). By contrast, others argue that economic power tends to have an adverse redistributive effect on wages and unemployment, thereby creating uncertainty for working people directly and for the economy indirectly (Pressman: 2006). It seems that there is a contradiction: reducing uncertainty on the part of capital heightens uncertainty on the side of labor. Whereas the first group, whose main focus is on microeconomics, does not go one step further and analyze the macroeconomic implications of economic power, the second group, which is interested in macroeconomic issues, does not explicate the rationale behind the
emergence of economic power in the market. As a result, there is a disconnection between the micro and macro dimensions of power and uncertainty in Post Keynesian economics.

The underlying contention in this essay is that market power, rather than solving the problem of uncertainty, fuels it by creating an unequal distribution of income, unemployment, and economic stagnation. Therefore, an activist state that takes care of the unemployed, poor, sick, and old lies at the heart of Post Keynesian economics. Competition, uncertainty, power, and freedom are the four solid rocks upon which the idea of a democratic welfare state established in Post Keynesian economics. While the first part analyzes the linkage between power and uncertainty in the market by outlining competition in the Post Keynesian tradition to show how economic power emerges and its effects on macro economy, the second section connects uncertainty to the democratic welfare state as the agent that can provide solutions to uncertainty for the capital as well as for the labor, before stating conclusions in the last section.

**Competition, Uncertainty and Power**

Defined as well-being or material and social prerequisites for well-being, welfare according to Christopher Pierson (1998), can be provided by three sources: social welfare, provided by the family, the church, and other charity organizations outside the market or the state; economic welfare, obtained through the market or the formal economy; and finally state welfare, services offered by the state. Accordingly, Pierson defines the ‘welfare state under capitalism’ as “a society in which the state intervenes within the processes of economic reproduction and distribution to reallocate life chances
between individuals and/or classes.” (p. 8) A key question to ask here is: Why does the state need to play a role to redistribute wealth in the capitalist market economy?

Answering this question requires establishing a linkage between competition, uncertainty, and power in the first place. Before defining and analyzing competition in Post Keynesian economics, it is important to define uncertainty and three forms of power—market, economic, political. Uncertainty is defined as “a situation in which people do not know the future and cannot rationally calculate what will bring them the greatest utility or what is in their own best interest.” (Pressman: 2006, p. 3) The absence of knowledge of future events at present is the source of uncertainty and decisions are made in historical times and changing them is costly from a contractual point of view (Monvosion & Rochon: 2006-7, p. 8). Power can reduce uncertainty, but cannot totally eliminate it (Monvosion & Rochon: 2006-7, pp. 21-22). Accordingly, Lukes defines power as A’s ability to control or influence B’s behavior through making decisions or not making decisions openly; through working behind the scenes to manipulate the agenda; or through persuading B to accept his/her agenda by shaping the perceptions and preferences of B of which B is not necessarily aware, even though they may be against or contrary to B’s own best interest (Lukes: 1974). Decision-making, agenda-setting and preference-shaping are the three main dimensions of power (Dyrberg, 1997). Giant business enterprises have resources and hence power to influence consumers’ and governments’ decisions directly as well as indirectly.

Analytical separation between market, economic and political power may further clarify the boundaries between politics and economics. Market power refers to the ability of an individual business enterprise or a group enterprises to influence price, quality and
the nature of a commodity in specific markets or in an industry in general (Montgomery: 1985, p. 790). Information is the source of power of business enterprises in Post Keynesian economics (Monvosion & Rochon: 2006-7, p. 22). By contrast, *economic power* is “the degree to which individuals or individual units affect the decision-making process.” (Klein: 1998, p. 394) What is meant by the decision-making process here is primarily political decision-making processes for deciding broader public policies. Economic power is broader in its scope and aims to influence public policies.

*Political power,* ‘a social power focused on the state’, is organizational power designed to coordinate the actions of people and promote the public interest (Neumann: 1950, p. 162). As such, it permeates all social activities in all spheres of life one way or another. In contrast to economic power that emanates from ownership, political power has its origins in people’s consent. Political and economic power are interdependent as well as intertwined. For Neumann: “Economics is as much an instrument of politics as politics is a tool of economics” (pp. 172–3). Despite the ontological separation between them, the boundary is blurred in day-to-day interactions. The next question to ask is: What is the nature of the relationship between competition and power in Post Keynesian economics?

Post Keynesians, according to Peter Kenyon, perceive competition as a process, not an end-state along with the classical and Marxian theories. Competition takes place through investment and capital accumulation (Kenyon: 1979, p. 40). Alfred Eichner (1979) describes the Post Keynesian vision of market competition as follows:

In a post-Keynesian analysis, competition need involve no more than a continual effort by business firms to exploit the most profitable investment opportunities. It is only competition in this limited sense that generally
prevails throughout the world – a fact that the classical economists clearly recognized (p. 16).

Business enterprises compete with each other on the basis of price and non-price elements to make a profit (Sawyer: 1994, p. 10). Profit is essential for their survival in the market in the long run (Lee: 2002, p. 122). Post Keynesians distinguish between two main forms of the market in studying the dynamic and complex processes of market competition. These are competitive and oligopolistic markets (Kenyon: 1979, p. 37; Steindl: 1952, p. viii). Competitive markets are not treated monolithically, though. Alfred Eichner further distinguishes three different types of competitive markets: Marshallian, Walrasian, and Chamberlinian. The non-oligopolistic subsector of the business sector consists of both polypolistic and monopolistically competitive industries (Eichner: 1976, p. 209). Nevertheless, they are prone to consolidation, especially the Marshallian markets.

In contrast to the existence of smaller firms of more or less the same size and similar cost structures in the Walrasian markets, there are recognizable differences in the size and cost structure of the firms in the Marshallian markets. Business enterprises have limited market power and hence control over the price level (Eichner: 1976, p. 132). Nina Shapiro and Tracy Mott (1995) characterize the Marshallian markets as an “imperfectly competitive industry.” (p. 36) Likewise, Nai-Pew Ong calls such markets a “stratified industry” whose main characteristic is that larger dominant, medium-sized, as well as, marginal firms exist side by side (1981, p. 114). Mainly new and developing industries can be an example of the Marshallian markets (Shapiro & Mott: 1995, p. 44). But this does not exclude a possibility that the Marshallian markets can also exist in consolidated industries (Hollander: 1961). Business enterprises ‘can often exert some
influence on each others’ price policy’ in large and open markets, especially in the manufacturing industry (Hague: 1958). As a result, market prices are erratic, flexible and uncertain. (Shapiro & Mott: 1995, p. 37). Naturally, business enterprises want power to control their market environment.

Most competitive markets evolve into an oligopoly “either as a result of consolidation from within…or through conglomerate expansion by megacorps seeking to maintain a certain minimum rate of growth for themselves.” (Eichner: 1976, p. 142) In other words, especially the latter is very unstable, and consolidation is inevitable. In contrast to the Marshallian markets, there are fewer big business enterprises, surrounded by some small or fringe enterprises in oligopolistic markets (Lavoie: 2002, p. 22). These big enterprises have similar cost structures and more or less the same amount of market power thanks to “the concentration of a large part of output in few hands.” (Steindl: 1947, p. 65) Nevertheless, monopolistic enterprises do not often use their power to compete on the basis of price in general.¹ Competitors can withstand price wars, which eventually hurt all players in the market, without any clear winner or loser in the absence of significant cost differentials among them. Price competition between business enterprises with similar market power and cost structures may be destructive without producing any conclusive winner. To avoid costly and destructive price wars, price leadership develops in such markets and all players follow the action of a small group of most powerful business enterprises in setting their prices (Shapiro & Mott: 1995, p. 43).

Competition still exists in oligopolistic markets in different forms. Business enterprises compete on the basis of mainly non-price elements (Rima: 1993–4; Eichner: 1983). Eichner and Kregel summarize the nature of competition in oligopolistic markets

¹ For pricing in Post Keynesian economics, see Lee (1998).
in the following words: “…competition is focused around investment, or discretionary expenditures, rather than around the price variable.” (Eichner & Kregel: 1975, p. 1305).

In oligopolistic markets, profit from investment is much more certain, while profit margins are higher compared to other market forms because of high entry barriers (Shapiro: 1992, p. 23). It means that oligopolistic markets are more stable and business fluctuations are more or less absent from the viewpoint of business enterprises. There are still casualties in that business enterprises with high cost structures are driven out of the market, especially when they face difficulties in financing their research and development efforts to offer new and innovative products (Lavoie: 2001, p. 27).

Overall, Post Keynesians contend that market power is essential for business firms to exert control over their environment in order to reduce uncertainty (Dunn: 2008, p. 178). “Like liquidity for the investor, power in the firm in many circumstances provides an insurance against an uncertain future for the capitalist.” (Stockhammer: 2006-7, p. 45) Power can reduce uncertainty by enabling business enterprises to control their environment. For instance, Virginie Monvoisin and Louis-Philippe Rochon explain the rationale behind why business enterprises need to control their environment more in uncertain times than in other times as follows:

If future levels of effective demand are not known—indeed if uncertainty is prevalent—then firms will want to exert as much control over their environment to guarantee their survival (i.e., the repayment of debt and the continued support of the banking system). In this sense, power is an important element of a firm’s survival: It will seek to lower wages, control costs, and impose a higher mark-up, among other things (Monvoisin & Rochon: 2006-7, p. 26).
Overall, regardless of their size, all business enterprises seek power, according Lavoie, to have control over their future (Lavoie: 1992, pp. 99-100).

It is clear that business enterprises solve the problem of uncertainty by reducing wages, cutting employment, and increasing mark-ups. Such measures, in fact, create more uncertainty in the future, as they cause a decrease in effective demand and unequal distributions of income. According to Steven Pressman (2007) who does yet to question why business firms amass power in the first place focuses on the adverse effects of economic power – which can be summarized as the amalgamation of market power of big business enterprises – for the economy, as it heightens uncertainty. As for the implications of economic power, Pressman makes the following observation: “More economic power for capital tends to reduce wages at the expense of profits. At the same time, greater power for capital affects government redistribution efforts, as the state reduces its support to the poor while at the same time lowering the taxes it collects from the wealthy.” (p. 26) Economic power, in fact, causes uncertainty by adversely affecting wages, employment, and government spending, thereby creating all the necessary conditions for economic stagnation.

If economic power decreases effective demand and uncertainty in the market increases, then business enterprises do not want to initiate investment in such an uncertain environment. “For Post Keynesians, uncertainty makes business firms reluctant to invest. This lack of investment, in turn, means that economies may find themselves experiencing prolonged bouts of unemployment, which requires the remedy of government macroeconomic policies.” (Pressman: 2006, p. 4) In other words, economic power is the principal force behind economic stagnation in oligopolistic markets. Power
solves the problem of uncertainty in the market by redistributing it to other sections of the society, especially to the working class initially. However, uncertainty on the side of labor becomes uncertainty for the capital indirectly later on, as effective demand decreases in the economy.

The situation in competitive markets is not very different from that in oligopolistic markets. Nina Shapiro (2003) describes the adverse affects of competition especially in Marshallian markets as follows:

Post Keynesians highlight the shortcomings of markets and the competition that regulates them. For them, as for Keynes, the competition of markets does not make them self-adjusting. It does not keep the demand for their products in line with the supply, or the supply in line with the labour available for its production. Labour can be unemployed, and products in excess supply, under competitive conditions also, and while the competition of firms can bring down their prices, it cannot keep up their production. Indeed, it may in fact ‘ruin’ them (p. 65).

In other words, market competition leads to uncertainty as a result of continuous instability. Under great uncertainty, business do not want to invest heavily or spend more. Besides, financial institutions also become reluctant to provide credit, if the rate of return from new investment is not certain. In short, intensive or cut-throat competition fuels uncertainty in the market for both business enterprises as well as for workers. The next question is: How can the problem of uncertainty solved?

**Freedom and Welfare State**

Post Keynesians perceive competition within a broader context instead of confining it to the market. The ethical dimension of competition is essential for the reason that it serves as a means of expressing freedom, but it is situated, not unlimited or negative, freedom. According to Edward J. McKenna and Diane C. Zannoni (1993):
“Freedom requires a social matrix for its existence, that is, freedom is situated freedom.”

(p. 405) Both individuals and business enterprises exist within a large social environment and hence have mutual rights and responsibilities towards each other. In that sense, freedom is both negative and positive. In other words, individuals require the absence of obstacles to express their freedom. Additionally, they need to have the necessary sources to take control of and realize their fundamental goals (Berlin: 1969). This is what situated freedom refers to. It is about the perception of individuals primarily as members of a community.

Shaun Hargreaves Heap (1989) establishes a linkage between freedom, power, and uncertainty and maintains that Post Keynesian economics has a specific perspective on welfare economics that favors egalitarian activism due to its emphasis on uncertainty.

Uncertainty is a testament to our social and historical location as individuals; it is the other side to a particular kind of freedom which can only be exercised through collective choices. Thus, post-Keynesianism sets the stage for an activist state by reminding us of our social interdependence; and egalitarianism would seem to be naturally associated with the recognition that such interdependence is central to social life (p. 161).

In the process of exercising freedom in both forms, the state is perceived to be an institution that helps mitigate uncertainty by ensuring a minimal level of future incomes (Pressman: 2006, p. 8). Welfare policies such as family or child allowances, more generous social insurance and pension policies, health care, and increasing ‘useful’ forms of government expenditure are some of ways to deal with economic redistribution to reduce uncertainty for individuals as well as for business enterprises (Pressman: 2007; Dunn: 2008, p. 185).
This brief sketch suggests that welfare state in Post Keynesian economics is has strong grounds. Pressman (2006) argues that:

The welfare state is based on the idea that it is not enough to rely on just the market plus family and social networks. Rather, for individuals to be able to take risks and spend their money (rather than save), they need some kind of guarantee that they will be taken care of during bad economic times (p. 28). \(^2\)

Nevertheless, policy outcomes depend not only on the state of the economy, but also on political factors and power relations between capital and labor, as both social forces struggle to redistribute uncertainty by using the state as an agent through the democratic process in the process of socializing uncertainty. This answers Engelbert Stockhammer’s (2006-7) criticism that the Post Keynesian tradition does not provide an “analysis of the state and the political and social coalitions on which state arrangements are based.” (p. 46) Overall, Post Keynesians attribute a positive role to the state in providing social safety nets, essential for both freedom of individuals and stabilizing the otherwise unstable capitalist market economy by reducing uncertainty.

**Conclusions**

This paper has indicated that the welfare state has strong theoretical foundations in Post Keynesian economics. It is established upon four pillars: competition, uncertainty, power, and freedom. In other words, the origins of the welfare state have its roots in the vision of capitalism. As an economic system, capitalism is a system that promotes creativity, initiative as well as innovation. To make the long short, left to itself the capitalist market economy generates instability and business cycles because of

\(^2\) See also Pressman, S. (2001).
destructive competition and waste. Post Keynesians believe that laissez-faire capitalism might be made to work.

The stability of the capitalist market economy requires an activist state which plays an active role in reducing uncertainty caused by competition and power, increasing confidence and improving economic performance through welfare state. In other words, the welfare state stabilizes the economy, while ensuring conditions necessary for the realization of individual freedom and continuous profitability. However, welfare state policies are not automatic. They depend on political factors and power relations between the social forces involved in the democratic process of policy making.
Bibliography


