Not since the Great Depression of the 1930s has it been so apparent that the core capitalist economics are experiencing secular stagnation, characterized by slow growth, rising unemployment and underemployment, and idle productive capacity. Consequently, mainstream economics is finally beginning to recognize the economic stagnation tendency that has long been a focus in these pages, although it has yet to develop a coherent analysis of the phenomenon. Accompanying the long-term decline in the growth trend has been an extra-ordinary increase in economic inequality, which one of us labeled “The Great Inequality” and which has recently been dramatized by the publication of French economist Thomas Piketty’s Capital in the Twenty-First Century. Taken together, these two realities of deepening stagnation and growing inequality have created a severe crisis for orthodox (or neoclassical) economics.

To understand the nature of this crisis of received economics it is necessary to look at the two principal bulwarks of neoclassical theory, which were originally erected in response to socialist critics. The first is the notion that a freely competitive capitalist economy left to itself generate full employment, indicating that unemployment is the product of various frictions, imperfections, or government interference. The second is the related proposition that income and wealth inequality are determined by the “marginal productivity” (or relative contribution to output) of the various factors of production, chiefly capital and labor- a logic that is extended to the contributions of individuals themselves. The renowned post-Second World War national income statistician, Simon Kuznets, in his famous Kuznets Curve, even argued that there was a tendency in developed capitalist economies towards a decrease in equality, due to the effects of modernization, including enhanced educational opportunities.

Contrast the proposition to the reality of the mature capitalist economies today. Far from full-employment equilibrium, what we see rather in a long-term tendency to economic stagnation. Moreover, this reality describes all of the developed capitalist economies and can be seen in a trend going back forty years, or indeed longer. Over roughly the same period, income and wealth levels, rather than converging, have diverged sharply- a divergence that cannot be attributed to differences in education and skill, or to the contributions of capital relative to labor. In short, both of the principal justification for the system provided by neoclassical economics has collapsed before our eyes.

The first of these fissures in the outlook of neoclassical economics is long-standing and well known. During the Great Depression, unemployment in the United States rose at its height in 1933 to 25 percent. It was in this context that John Maynard Keynes, the intellectual heir to Alfred Marshall at Cambridge University, and hence one of the principal figures in neoclassical economics, broke partially with the economic orthodoxy with the publication of his magnum
The Crisis of Neoclassical Economics (Part I)

opus, The General Theory of Employment, Interest and Money in 1936. Keynes sent mainstream economics into a tailspin by attacking (as has Matrix earlier) the notion of Say’s Law of classical economics, which postulated the supply creates its own demand. He thus engaged in a frontal assault on the notion that full-employment equilibrium was an inherent tendency of the system. Instead Keynes contended, “When effective demand is deficient there is under-employment of labor in the sense that are men who are unemployed who would be willing to work at less schooling and training); and eventually, the above average wage-cost difference will disappear. Remarkably, this theory shows that, while some workers earn higher wages than others, these higher wages simply reflect higher entry costs. A doctor is therefore not really off than a motel room cleaner; in terms of wages minus costs, they are in exactly the same position. Voila! At least as far as labor income is concerned, there can be no inequality.

Enter the real world. The Great Financial Crisis of 2007s and the Occupy Wall Street uprising punctured this neoclassical fairy tale. The Occupy movement pinpointed the growing division between the 1% and 99%-achieving in a very short time a transformation in public consciousness on inequality that radical political economists had sought to effect for decades. The press began to draw more frequently on data showing skyrocketing income and wealth inequality that had long been available but had been relegated to the status of a dirty little secret of the capitalist economy. For decades researchers had been compiling sophisticated statistical portraits in the area. Now due to Occupy and the sheer outrage of the population, it all began to come out into the open.

Yet, the big change of the data front, making it impossible to deny any longer the extent of the growth of inequality in all of the mature economies was the development, over the last decade and a half, beginning with the early work of Piketty, of the World Top Incomes Database. The result of a major international project, involving some thirty researchers, this database primarily uses income tax data, focusing on most of the mature capitalist economies. The leading researchers for the US case were Piketty himself, located at the Paris School of Economics. The Top Incomes Database is the single largest historical database on long-term inequality currently in existence, covering countries in Europe and North America, but also a sampling of countries in Asia, Africa, and Latin America.

The publication of Harvard University Press in 2014 of Capital in the Twenty-First Century by Piketty, using the Top Incomes Database to explain the dynamics of growing inequality at the center of the capitalist world. For Piketty is no ordinary economist. He is at one and the same time a dissenter and a representative of the higher circle of the economics establishment.

For most readers it was not the fine details of Piketty’s analysis that were so interesting but
rather the overall conclusions dramatically highlighted in the very beginning of the book. Here he made it clear that he was challenging head-on some of the core assumptions of orthodox economics—though from inside rather than outside of the neoclassical perspective. It was this divorce of his analysis from the main ideological propositions of received economics—the sense of letting the numbers speak for themselves—that gave Piketty’s work the feeling of a disinterested inquiry after the truth rather than what Marx called “the bad conscience and evil intent of apologetics” that has long dominated orthodox economics.

Most importantly, Piketty concluded in what will undoubtedly be his single most enduring contribution, that “There is no natural, spontaneous process to prevent destabilizing, inegalitarian forces from prevailing permanently” in capitalist economy. This can be seen as the critical counterpart to Keynes’s break with Say’s Law, or the notion of a natural tendency to capitalism to full-employment equilibrium. Not only does Piketty point out that Kuznet’s assumption of growing equality in developed capitalist economies is wrong, but he argues that the standard neoclassical human-capital argument of equality-cum-meritocracy—wherein deviations from equality are simple due to attributes such as greater skill, knowledge, or productivity—is equally false in the real-world economy.

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By: John B. Foster and Michael D. Yates