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**Foundation Day Lecture of**  
Omeo Kumar Das Institute of Social Change and Development



**Current Crisis in Capitalism**  
**A Brief Outline and a Way Forward**

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# **Current Crisis in Capitalism**

## **A Brief Outline and a Way Forward**

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## I. Preliminaries

Dear friends: I deem it a great honour to have been invited by the Acting Director of OKDISCD, Professor Saswati Choudhury, to deliver this year's Foundation Day Lecture. OKDISCD is a major, and well recognized, institution of India that is engaged in meaningful social science research in the areas of regional development, governance, livelihood and environment, health and education, ethnicity, peace, conflict and gender issues, among others. The institute is named after Omeo Kumar Das, visionary freedom fighter, writer, political leader, and the first Education Minister of Assam. He was also an eminent Gandhian scholar. It is to his memory that this lecture is dedicated.

I now come to the theme of my lecture.

It would be no exaggeration to assert that the dominant political economic system across the globe today is that of the capitalist market system. Even the most prominent communist regimes of Russia and China have also, in recent years, embraced the market system and seem to be increasingly comfortable with the capitalist ethos. Yet, while capitalism today rules the roost as the principal economic system, a natural question arises as to whether it may be regarded as being an ideal system, one that is free of blemishes. The answer, as known very well, is in the negative. Yet we are witness to the continuing sway of the capitalist system, and this must therefore be regarded as a conundrum.

In his magisterial work 'Capitalism, Socialism and Democracy', published in 1942, Joseph Schumpeter asked the question, 'Can Capitalism Survive?', and proceeded to provide the answer himself: 'No. I do not think it can.' (p. 61). More than eight decades have passed since Schumpeter's most widely read and quoted work. In all fairness, Schumpeter had not suggested any particular time horizon for this process to fully play out. So, what we have is that the incumbency

of capitalism continues with some major and minor hiccups and with several spectacular innovations and technological breakthroughs, all of which are par for the course for the capitalist system.

It is difficult to come across, historically, any other economic or political thinker who extolled the virtues of capitalism as accurately, comprehensively, and with exceptional foresight, as we see in the case of Joseph Schumpeter. By common consent the most spectacular success that capitalism ever achieved was during the Gilded Age, or the Belle Epoque, roughly covering the years following 1870 up until 1914, the start of the First World War. These were the years in which the telegraph, the telephone, electricity, long distance oceanic shipping, the rail network in Europe, North America and the Indian subcontinent, and mass production of automobiles for the common man, came on with astonishing rapidity.

Schumpeter was 28 when he published *The Theory of Economic Development* in 1911. This was a tract on the development experience of the advanced capitalist countries, viz., England, the United States of America and Germany, in the main. In his view, the development process in a free market capitalist economy is driven by the paramount role of the entrepreneur who combines factors of production to produce goods that would have a demand in the market, enabling him or her to earn a profit. The more innovative the entrepreneur, the higher the quantum of profit would be. The entire capitalist process is one where there is a perennial gale of creative destruction, where established products become obsolete, making space for newer and more novel products. One can hardly think of a more apposite description of the modern world of information technology and artificial intelligence than this description by Schumpeter.

The above paragraphs would seem to suggest that the capitalist market system has much going for it, and it would seem to be seemingly invincible. That indeed was the presumption of the classical school associated with the names of Adam Smith, David Ricardo and Jean Baptiste Say, among others. The large body of their thoughts is often referred to as the Smith-Ricardo-Say system. One of the key elements of this system was the belief that the market system is self-regulating, and that it is one which would always ensure the full employment of all factors of production, including labour.

## II. Instability in Capitalism

The classical system was in for a rude shock following the Wall Street crash of 1929, leading up to the Great Depression. Within a span of two to three years the capitalist system appeared to be grinding to a halt, as unemployment rates in the US and UK economies touched the 25% mark. Hardship among the poor and the working class in these most advanced of economies reached alarming proportions. It is in this setting that the iconoclastically original mind of John Maynard Keynes came up with his 'General Theory' (1936) that altered the understanding of the economic reality in unprecedented ways.

One of the fundamental features of the classical system was the notion of equilibrium and the belief that the inherent proclivities of economic agents in their roles as consumers and producers would ensure that the market mechanism would always work with full employment of all factors of production. Keynes however posited that the presence of certain kinds of rigidities, especially in the labour market, might bring about an equilibrium of the system at less than the full employment level. This was a revolutionary departure from the basic structure of the Smith-Ricardo-Say framework. The problem, in Keynes' view was arising because of inadequacy of aggregate demand. What was to be done to redress this? Keynes prescribed increased government spending, even, if need be, via printing currency notes. This was anathema to the purists among old style theorists and conservative bankers. But this indeed was the perfect antidote for an economy that had excess plant capacity that was lying idle simply owing to low effective demand.

Among the major classical thinkers, Malthus was the lone person who had foreseen the possibility of slumps in market driven economic organizations, but his cautionary views were at variance with the extensive appeal of the classical system which supported *laissez faire*, and saw little merit in any intervention on the macroeconomic front by the government. Keynes saw himself as a legatee of the 'first Cambridge economist', Thomas Robert Malthus. It is from Malthus that Keynes got the phrase, and possibly the idea of, 'effective demand'. From the autumn of 1931 to the summer of 1935, Keynes worked on a new book on macroeconomics, initially entitled 'The Monetary Theory of Production'. In 1935 Keynes had written a letter to George

Bernard Shaw: 'I believe myself to be writing a book on economic theory which will largely revolutionize – not, I suppose at once, but in the course of the next ten years – the way the world thinks about its economic problems' (see Keynes (2015), p. xx). The 'General Theory of Employment, Interest and Money' was published in February 1936.

Keynes was quintessentially a liberal democrat and any notion of socialism, and more so communism, was deeply antithetical to his closely held beliefs. He was dismissive of Karl Marx's worth as an economist. He also held that of all conceivable political economic systems, capitalism is the one with the least faults, and his lifelong project was to ensure the workability of capitalism. It is possible to hold the view that Keynes was able to singlehandedly plug the problem of instability that continually haunted the capitalist system. Clearly he had been able to do this by thinking out of the box. It possibly helped that in his academic training Maynard had not learnt economic theorizing in the tradition of Smith, Ricardo, Mill or Marshall. Maynard's formidable brilliance was well known to his teachers and contemporaries. At Cambridge Keynes sat for the Mathematical, not the Economics, Tripos examination in May, 1905, coming out as twelfth wrangler. It is only in the summer of 1905 that he, then 22, turned his attention to studying economics under the tutelage of Alfred Marshall.

If instability was possibly the single biggest and reluctantly acknowledged issue with capitalism, at least post the Great Depression of 1929-33, there are at least two other major difficulties with the capitalist system that need to be addressed head on. The first is an old and fundamental issue that has been at the heart of great historical revolutions, to wit, the issue of inequality in the distribution of income and wealth. The second issue too has been there all through the process of capitalist development, but had not been acknowledged to be a problem worth a serious consideration till about a hundred years ago. It is the issue of environmental degradation and climate change, which has come into the public focus only in the recent decades. We shall address these issues in turn.

### III. The Market Mechanism

The key to understanding the capitalist system is to examine the working of the market mechanism as well as the use of the banking system and

financial mediation by the entrepreneurial class. Up until the prevalence of the monarchical system and feudalism, productive activities were limited to the initiatives of individuals or groups from the landed or feudal aristocracy who could provide their own finances to branch out into non-farm activities. The middle of the eighteenth century witnessed a number of path breaking technological breakthroughs, especially in England, which included, notably, the steam engine, and the spinning jenny, among others. Parallel to this there was the rise of the modern banking system based on the principle of fractional reserve requirement. Because of the ease of borrowing of finance capital from the banking sector, there was a rapid rise of the entrepreneurial class. In contrast to feudalism, capitalism saw the rise of a labour class which was available for factory work in exchange for wages.

Adam Smith's 'Wealth of Nations' (1776) was published when the Industrial Revolution was in its beginning stage. The key to the dynamism of capitalism was the phenomenal rise in production possibilities owing to technological breakthroughs. These were facilitated with the process of specialization via division of labour. Smith was possibly the finest representative of Scottish moral philosophy, and one who believed that the best way to organize social and economic activity is to allow individual agents, in their role as producers and consumers, to pursue their self-interest to the fullest. He asserted that this would lead to harmonious results for the economy and the society at large, and that this would be ensured via what he called 'the invisible hand'.

Smith's invisible hand pointed at two implications. The first was that a competitive market economy, comprising of atomistic consumers and producers, can be expected to be in a state of equilibrium, which is to say that the combined actions of innumerable economic agents will be in balance. In formal terms, there will exist a price vector of all goods and services which will precisely clear all markets, in the sense that there will be no excess demand or supply of any good. This is the so called problem of the existence of a general competitive equilibrium. In more elaborate terms, if all consumers are maximizing their utilities subject to their budget constraints, and all producers are maximizing their profits subject to the available factors of production at their command and technology, then, under certain reasonable conditions, there will exist an equilibrium price vector that would clear all markets.

The proof of the existence of competitive equilibrium is not a trivial exercise. The finest economic brains through the nineteenth and much of the twentieth century were engaged in this task. Possibly the most outstanding of them all was Leon Walras (1834-1910) of the Lausanne school. However, the most general proof of this problem was finally provided in two pioneering papers, one published by Lionel McKenzie in the *Econometrica* of March 1953, and the second, jointly authored by Kenneth Arrow and Gerard Debreu, published in the June number of *Econometrica* in the same year. These two papers established for the first time, in rigorous and most general terms, that the original idea of Adam Smith's invisible hand had a firm foundational basis.

There is however another, deeper, issue. This concerned the issue as to whether a competitive equilibrium allocation can be expected to have any welfare properties. Is the competitive equilibrium a good or bad outcome? Arrow and Debreu went on to prove two results which are today known as the two fundamental theorems of welfare economics. The first theorem demonstrates that all competitive equilibrium allocations are Pareto efficient. An allocation is Pareto efficient if no single individual can be made better off without hurting the lot of at least one other individual in the system. This is a theorem about the efficiency of the market system.

#### IV. The issue of Equity

What about equity, or distributive justice? The second theorem addresses this question. The statement of the theorem goes as follows: Under certain conditions that have to do with the convexity of production sets as well as convexity of preferences, any arbitrarily chosen Pareto efficient allocation can be achieved as a competitive equilibrium with suitable initial transfers. Amartya Sen has remarked that the second theorem could be thought of as being from a revolutionary's handbook. The key to this theorem is the requirement of 'suitable initial transfers'. If there is an omniscient state that has the power to appropriately take away property or endowment from the rich and award it to the poor, then any ethically desirable Pareto efficient allocation can be supported as a competitive equilibrium allocation.

The second fundamental welfare theorem allows us to separate the issues of efficiency from those of equity. The big 'if' concerns the issue

of whether the state can confiscate property or endowment from any individual in a capitalist system, or whether property ownership is sanctified by a legal and juridical process. In most liberal democracies property ownership is protected by the state. Economies that are characterized by deeply skewed distributions of income and wealth are typically fortified by the upper or richer strata who are protected of their property ownership, in which the political and judicial systems are usually complicit. To put the matter in other words, highly skewed distributions of income and wealth may continue to remain so for decades, or even centuries.

Would it be possible to aim for a society or economy with a perfect equality of income and wealth for all agents? No liberal democratic system would support it, since it would violate individual free choice. It may seem paradoxical, but Marx, too, did not have any special fascination for an economy with perfectly equal income. What he ultimately argued for was a classless society without any social or economic hierarchy. As regards distribution he was in favour of Louis Blanc's precept: From each according to his ability, to each according to his needs.

#### V. Inequality

The problem still remains that the capitalist system is inherently one that is built on those processes that give rise to increasing concentration of income and wealth. If one imposes the rule of equal income by fiat, the whole notion of the 'magnificent dynamics' of capitalism would be lost.

A substantial body of the work of Thomas Piketty points to rising concentration of income and wealth in the mature capitalist economies of Western Europe and North America. One of the policies that Piketty has lately been suggesting is the imposition of a wealth tax. A very serious evaluation of the possibility of a wealth tax is definitely now the need of the hour.

According to a recent report by the World Inequality Lab, India's top 1 per cent income and wealth shares have reached historic highs and are among the very highest in the world. In 2022-23 the share of the top 1 per cent accounted for 22.6 per cent of the income share and the share of the wealthiest 1 per cent was 40.1 per cent. The income share of the top

1 per cent in India was higher than the corresponding figure for South Africa, Brazil and the United States. The report goes on to suggest that a 'super tax' of 2 per cent on the net wealth of 167 wealthiest families in India would yield 0.5 per cent of national income in revenues and create space for investment.

Perhaps the single greatest problem with the capitalist system is its proneness to the concentration of income and wealth. It is this which was at the heart of its rejection by Karl Marx. Marx's object was to understand and unravel the inner workings of the capitalist process. He established that the entire capitalist system is based on the realization of surplus value by the owners of capital, and that labour would necessarily be at the receiving end of the exploitative process. As the system progresses it would lead to a greater and greater degree of immiserization of the work force. The system would ultimately implode and the working class would then wield the levers of power.

Even though the Marxian scenario has not exactly worked through in the advanced capitalist countries of Europe and North America, the issue of high and growing concentration of wealth is a reality. One possible antidote to the growing inequality of income is to provide free education, health and social protection to the bottom rungs in the society.

## VI. Ecological Degradation and Climate Change

Some 248 years after Adam Smith's 'Wealth of Nations' the world is at an important crossroads. Smith had never conceptualized the issue of pollution, or environmental degradation. The world was substantially in its pristine form. Within a matter of 22 years after Smith's work, Malthus in 1798 alerted the English people about the possibility of food scarcity. His argued that while food output grew in arithmetical progression, human population grew in geometric progression. Malthus's friend David Ricardo soon pointed at the possibility of land scarcity as the need for food grains increased along with the increase in population. Both Malthus and Ricardo contributed to defining economics to be a study of scarcity.

By the 1840s the industrial revolution in England had brought forth unprecedented changes in the labour force. Large swathes of peasants left their agricultural farm lands to gather at the industrial townships

of London, Manchester and Liverpool. Working conditions were bad and living conditions extremely poor. The living conditions of women and children were atrocious and alarmingly exploitative. It is in this background that Marx and Engels penned 'The Communist Manifesto' in 1848.

As has been mentioned earlier, sometime around the 1870s, a century after Adam Smith's 'Wealth of Nations', England entered a phase where the gains due to capitalism's dynamism and technological innovations were slowly spreading to the common work force, and the next forty years witnessed unprecedented improvement in the living standards of working class. This was also true of Western Europe and North America.

The dynamics of capitalism were built on the exploitative use of the world's forests, water resources and fossil fuels. This was already causing substantial damage to the environment and ecology. Most economists were however unmindful of this. John Stuart Mill was an exception who argued for a 'stationary state', and cautioned against the exploitative use of nature. He argued for human beings to be concerned – after the essentials of day to day living were taken care of - with the issues of liberty, justice and suggested that they should have more leisure develop their mental and moral capacities.

It is only in 1920, a bit more than a century back, that the Cambridge economist Arthur Cecil Pigou wrote a justly famous tract called 'The Economics of Welfare'. In it Pigou developed the concept of externalities from Marshall and used it to justify government intervention. Urban squalor in the industrial townships of Birmingham, Manchester and London were already quite apparent by the 1850s to social realists like Charles Dickens who wrote 'Hard Times', the tale of a group of people living in an industrial town called Coketown. Yet the discipline of political economy had not been sensitized enough to address the issue of pollution and environmental degradation head on and it took another 70 years for Pigou to emphasise its deleterious role in worsening human welfare.

Pigou drew attention – in the context of externalities – to the divergence between private cost and social cost. This also meant that externalities would typically lead to market failure. In the case of steel production by a factory that is emitting foul smoke into the atmosphere, the private

cost of producing the good is only one part of the cost. The other, social, cost is the damage to the surrounding atmosphere and the health of the residents living around the factory. Private, profit maximizing, producers would produce steel up to the point where the private marginal cost is equated to the private marginal benefit. Pigou suggested that producers must be made to produce where the social marginal benefit equals the social marginal cost. This may be brought about by suitably calibrating a Pigouvian tax that would curb the output of steel appropriately, without banning steel production altogether.

Interestingly, this central idea of Pigou took almost a half century to be adequately appreciated by policy economists in the major capitalist countries of the world. It is only in the 1970s and thereafter that environmental economics came to be recognized as a major area of study in the American and European campuses.

In more recent years climate change has emerged as a major issue, or rather a crisis, that confronts the entire globe. As such, this refers to a long term change in the average weather patterns that have come to define the earth's local, regional and global climates. The main driver of climate change is the burning of fossil fuels like coal and oil which produces heat-trapping gases. This has been happening from the beginning of the industrial revolution, and especially from around 1800 AD, and the major industrial powers of Western Europe and North America have been the principal contributors to the earth's stock of greenhouse gases.

In his ground breaking report, Lord Nicholas Stern of the London School of Economics has concluded that climate change is the biggest market failure the world has ever seen. Carbon pollution has imposed massive social costs, but emitters have so far faced little incentive to cut back. Left unchecked, Lord Stern argues that climate change would have adverse impacts on food production, access to water, and human and animal health. Water shortages, coastal flooding and hunger could affect hundreds of millions of people, disrupting life on a scale even more severe than the world wars. These costs may well be equivalent to losing 5 per cent of global income every year forever. The Stern Review concludes that by spending a much smaller amount – about 1 per cent of global income – the greenhouse emissions could be substantially reduced. The benefits of acting now clearly outweigh the costs.

## VII. The Perspective from India's Standpoint

It would not be inappropriate to say that the Indian economy today largely works along the framework of a capitalist market system. Our political economic developments have been such that we have substantially abandoned the old style planning set up where the Planning Commission oversaw most of the large investments in infrastructure and core industries. In 1991 the country went in for substantial economic reforms while retaining the Planning framework, but soon after the beginning of the NDA regime in 2014 the Planning Commission was wound up, and replaced by a new policy think tank called the NITI Aayog.

Among the severest challenges facing the country are the problems of unemployment and accentuating inequality. It is possible to suggest here that for addressing our age old problems mentioned above, along with the continuing problems of poverty, ill health, poor quality of education, and in particular, poor maternal and child health, we possibly ought to think along our homegrown approaches rather than simply aping the practices of advanced countries.

It might be instructive to seriously consider some of the thoughts of Mahatma Gandhi on the issue of development. Gandhiji had put down most of his core thoughts in 'Hind Swaraj' published in 1909. Some of his main ideas centered on (1) placing the maximum focus on developing Indian villages as self-sufficient units, (2) ensuring that all able bodied adults are actively employed, (3) minimization of human wants, (4) the notion of trusteeship and (5) the need to focus on the welfare of the 'daridranarayan'- the worst off member of society.

The idea of minimization of wants is the exact obverse of the classical and neo-classical economists' perennial emphasis on expanding the production possibility frontier to limitless lengths. Gandhiji's ideas would be more consistent with our present day ecological imperative to protect and sustain resources. The idea of focusing on the well-being of the daridranarayan is none other than the Rawlsian principle of doing the best for the worst off member of society. Gandhiji had independently thought of this ethical principle well before Rawls articulated his views in the 1950s, which were elaborated further in his magnum opus, 'The Theory of Justice' (1971).

Important intellectual formulations were put forward by Nehru and Rammanohar Lohia, among many others. Nehru's emphasis on higher education and the establishment of the IITs, IIMs and the AIIMS in the 1950s has offered us an invaluable system of public funded higher education that has stood us in good stead. We do not seem to be adequately cognizant of its benefits today. Lohia believed that the examples of American capitalism as well as the communism of USSR were equally irrelevant in the Indian context. In order to ensure full employment for all, he believed that we need to focus on appropriate, small scale equipments and implements, for our teeming masses.

Despite significant progress on several fronts in recent years, India's deep developmental problems continue to remain and much interest is attached to how we are able to engage with these problems in the coming decades.

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