

THE CANADIAN JOURNAL OF
ECONOMICS AND POLITICAL SCIENCE

Volume II

MAY, 1936

Number 2

ECONOMIC THEORY AND NATIONAL PURPOSE

AS time goes on the full scope of the National Socialist movement in Germany becomes apparent to the outside world. The abolition of democratic institutions and the assumption of supreme power by the *Führer* were not surprising in principle to observers in foreign countries, though they were startling to many in their completeness and ferocity. Similarly, we were more or less prepared for the withdrawal from the League of Nations, and the changes in foreign policy associated with it. But I do not think it was generally expected that the movement would include a reform of education, not in such matters as methods of teaching but in regard to the content of the subjects taught. To those who are accustomed to regard the truth or falsity of the subject-matter of education as independent of the political character of the government this comes as something of a shock. A remarkable series of pamphlets under the general title *Der Deutsche Staat der Gegenwart* deals with some of these "reforms", particularly as applied to the subjects of law and economics. Volume XV of the series is entitled *Das Studium der Wirtschaftswissenschaft* and describes the new curriculum of economic studies. It gives the new curriculum itself, in some detail, and contains, as well, addresses by Professors Dr. Eckhart, Gottl-Ottlilienfeld, and Wiskemann which reveal, sometimes as through a glass darkly, the ideas underlying the "reform".

Perhaps the keynote of the whole matter is struck by Professor Dr. Eckhart's declaration that "German economic science must become national socialistic". This means that German economic science must be dominated by a political point of view and that one of its objects, if not its main object, must be to educate students in the principles of National Socialism. Ideas of the same sort, it would seem, found expression in the reform of legal studies which preceded the reform of economics. Indeed, economics and law are regarded by the National Socialists as such closely related subjects that the possibility of having a common curriculum for both was

seriously considered. This was decided against, but the two courses of study, as reformed, have much in common.

This extreme association of law and economics itself indicates something of the nature of the new curriculum of economic studies, and suggests the dominance of ideas of a political character. But we have more positive evidence than this. There is, for example, the statement by Professor Dr. Gottl-Ottlilienfeld that "Law participates in every formation of economy. Whoever has to do with economy, whether intellectually or practically, as a theorist or as a man of affairs, must see to it that in the formation of the economy the true law is honoured." Or again the statement, this time by Professor Dr. Wiskemann, that "Our effort must be to found a genuinely political theory of economy". Liberalism and Marxism, Professor Dr. Wiskemann goes on to say, were political but in a different way, since they were concerned with "material quantities".

The National Socialist economic theory on the other hand is determined by (bestimmt) striving and creating humanity. It is not composed of natural laws, in the sense of the natural law which rules dead objects. It is charged with the spirit of the people, which follows biological and historical laws, which have the Will and the Idea as starting points. It is the heroic spirit, which the Nordic peoples have taken for themselves as the true clue; that spirit of work, of duty, of complete devotion to the community. . . . Only within the framework of this supreme national purpose does the question interest us what effects particular measures normally have in the domain of economy *i.e.* economic theory in the narrow sense.

There is a good deal of nonsense in this, of a sort which makes the writer of this article feel like uttering a vulgar ejaculation; but it will serve, perhaps, to illustrate the point about the influence of political ideas on the new German economics.

When we try to find, in the pamphlet, the answer to the question of precisely *how* the new economic theory is to differ from the old, what principles are to be discarded as false and replaced by new ones having Nazi approval, we are left in doubt. For that we will have to wait until the new books covering the field of economic science from the National Socialist point of view, which are undoubtedly in course of preparation, have appeared. We are, however, informed that the study of "Volk und Wirtschaft", which forms part of the work of the first semester, "should show that economy is not to be understood from the market or the enterprise, but from the people". "Foreign trade", also, "is not simply the theory of the world market, but treats all economic processes which reach across national borders as a part of the national economy itself." Again, regarding the study of money and credit, it is to be "no money and interest

theory in the capitalistic sense; it treats, much more, in general and from the standpoint of the German economic system, how the characteristics of currency and credit are built up within it, and what functions they fulfil. As supplementary study the seminars concern themselves with the technique of the field." Professor Dr. Wiskemann helps us to form an idea, too, of what the new economic theory will be like when he criticizes the old by saying that it produced

the social scientifically trained supporter of interests and the merchant coated with the whitewash of economic theories. . . . Economic theory had become—it sounds almost a contradiction—a burden from a materialistic generation, which out of the striving for a general profit maximum produced nothing but oppositions of interests and classes. Thus the natural and moral order of life of the people was split at the root. The revival of our subject could come about only through Adolf Hitler and . . . National Socialism, which once again gave to us in Germany the possibility of a national, political community life. The reform of studies which lies before you is nothing but the logical result of the spirit and form of National Socialism, applied to the science of the needs of life on the one side and the forces of life and action on the other, which we are accustomed to describe as Economic Theory.

Later on, when he is considering the new curriculum somewhat in detail, he says, "the second semester brings a two or three-hour course of lectures under the title Economic Theory, which is accompanied by a two-hour seminar Here belongs the theory of the form and movement of economy, including the theory of production and consumption, exchange and money, income, capital and interest theory, *all seen in a new theoretical connection*" (italics mine). With these hints we must, for the present, be content.

Now much of all this has a familiar ring. We have been accustomed at least since the days of Friedrich List and the writers of the Historical School to hear much about "Volk", and historical stages, and customs, and national forces, and the connection between all of them and economic theory. Students of the history of economic doctrine will doubtless find it easy to show the relation between the present ideas and those that preceded them, and prove that the former are merely a development of the latter. Nevertheless they are a development, and in some respects a considerable one.

I suspect that economists in British countries and in the United States are apt to contemplate the present position of economic studies in Germany as revealed, for example, in this pamphlet, with a considerable degree of complacent satisfaction associated, no doubt, with a feeling of sympathy for their unfortunate German fellow students. "Economics has then as its purpose", says Marshall, "firstly to acquire knowledge for its

own sake." They may naturally think great thoughts about Freedom—the advantages of free institutions, freedom of thought, "Lehrfreiheit". They may even formulate vaguely in their minds some sentences about the genius of the Anglo-Saxon (I hope they will not say Nordic) race in this respect; sentences which may even bear comparison with those of Professor Dr. Wiskemann quoted above. To what extent is such a feeling of superiority justified?

It is not my intention to discuss in this connection, though it would be relevant and interesting to do so, the extent of political influence on education, especially university education, and more especially education in the field of economics, in British countries and in the United States. But I fancy that no one who has any acquaintance with the facts will deny that it exists. Neither shall I discuss, although that also would be interesting and relevant, the extent of other external influences comparable to the political, such as that of the propertied class. But does anyone deny that this also exists? What interests me more, and what I do propose to discuss briefly in what follows, is the more general question of the influence upon economic theory of ideas of a purposive nature as to what ought to be *done* in the domain of practical life. The proper relationship between science and practice would seem to be that practice should be deduced from science; that certain things should be done *because* certain things are true. What I am suggesting is that in a good deal of economic theorizing this relationship is reversed, and what is represented as science is deduced in the last analysis from ideas or convictions about the wise course of action in relation to certain practical problems. Let us consider some examples.

The student of the theoretical parts of *The Wealth of Nations* may linger long over the distinction between "Productive and Unproductive Labour". The point of it, as I read the passage, is not the difference between the sort of labour which "fixes and realizes itself in some particular subject or vendible commodity", and the sort which does not, although that certainly is the way the discussion is introduced. The author goes on immediately, however, to the subject of different kinds of consumption and distinguishes between the kind that maintains or increases capital and the kind that does not. Further, we are told that "That part of the annual produce of the land and labour of any country which replaces a capital never is immediately employed to maintain any but productive hands". In short, the whole passage seems to me to be a discussion of the topic more familiar to present-day economists under the title "Productive and Final Consumption", or "Investment". But why did Smith call "unproductive" the sort of labour which yields final satisfaction, and "productive" the one which maintains or increases capital? Was it because, like a true Scot, he

approved of thrift? Was he, unconsciously of course, building up what purported to be a scientific distinction to support a policy in which he believed?

Another fascinating discussion in *The Wealth of Nations* is that "Of the Different Employment of Capitals". Why did Smith argue that the employment of an equal capital in different ways supported unequal amounts of productive labour and added unequal amounts to the wealth of the country? The argument is not consistent with his theory of value (any of them!) or with most of what he says about the nature of capital. Moreover, it is inferior in logical consistency to what we are accustomed to expect from his pen. Is the explanation, here also, that he held firm convictions on certain disputed questions of economic policy, about which he intended to have much to say in the two following books; that he believed, though to a lesser degree than his Physiocratic friends, in the superiority of agriculture, and disbelieved in the policy of protection; and that he built up a "scientific" structure with which he could defend the one and attack the other?

This concept of capital was also the occasion of considerable difficulty to John Stuart Mill. Although he attached great importance to it, and wrote no less than three chapters on it in book I, he was never clear about it. One of the worst arguments in the entire length of the *Principles of Political Economy* is contained in book I, chapter v, section 9. There it is argued, at great length and with a profusion of illustrations, that demand for commodities is not demand for labour. The whole performance seems to me to invite, and indeed demand, explanation especially coming as it does from a man of no mean intellectual power and a famous logician. The whole argument is, of course, all of a piece with the Wage Fund Theory which makes its appearance in book II, chapter xi, section 1, and which is now being revived under distinguished patronage. But why did Mill go to such pains, and such length, in his discussion of capital, to build up an argument which he was certainly capable of seeing was fallacious, and to support it by an unusual number of spurious examples cunningly devised to make the argument appear plausible, in order that he might later on consistently advance the Wage Fund Theory to "explain" wages? The latter is, of course, not an explanation at all, at least in the form in which Mill gives it (I say nothing about the new doctrine under distinguished patronage), but a statement of the problem.

These are all questions of interpretation, to which no certain answer can be given. Preference must fall upon the answer which, while admissible in other ways, makes sense of what is otherwise unintelligible. The interpretation which is here suggested is that Mill held strong convictions, not

the product of his reasoning on economic theory, on a number of debated questions of economic policy, especially population and the institution of private property. Perhaps his opinions on these questions were hardened by discussions in the study group which he describes in his *Autobiography*. Like the good mid-Victorian bourgeois that he was, he believed firmly in private property and the beneficent influence of the capitalist upon the community and especially on the labouring class. Moreover, he disapproved of poor people having large families (one almost suspects that he disapproved of families altogether), and believed it would be wise policy on their part as well as good for the community if they had fewer children. He was, in short, one of the early believers in birth control, though he probably would not have approved of some of the methods now both advocated and applied. Perhaps the alternative title of "family planning" would better suggest his views. Holding these convictions, Mill was led to argue, following, to be sure, the teaching of his father and of Ricardo, that demand for commodities was not demand for labour; that the latter depended entirely on the size of the wage fund, which depended, again, on the accumulation of capital; that a transfer of demand from the direct services of labour to commodities produced by labour diminished the total demand for labour and was injurious to the interests of the labouring class; and that wages were "explained" by saying that they depended upon the proportion between the wage fund and the number of labourers.

A somewhat analogous instance is to be found in the ancient and honourable Quantity Theory of Money. This theory is often associated with "equations of exchange" of one sort or another, though it is not always clear whether the equations are regarded as proving the theory, or are known to prove nothing and are used simply as a device for exposition. Mr. Keynes, fortunately, is explicit on the point, though he has no particular concern for the Quantity Theory. The fact of the matter is that equations of exchange are merely algebraic expressions which relate to each other certain economic factors which are regarded by the author as significant for the problem in hand. The quantity of money is usually one of these factors, and the price level another. The relationships between these factors, however, are not such that any one factor, while influencing the others is itself uninfluenced by the others. The quantity of money, for example, while it exerts an influence on the price level, is itself influenced by the price level. The factors which are brought together in equations of exchange, and the statement is true of economic factors generally, all react on each other. They are causes and effects at the same time. What justification is there, therefore, for explaining one of them, say the price level, in terms of another, or others, say the quantity of money or the quantity of

money and its velocity of circulation, rather than *vice versa*?

Can justification be found in historical facts? Is it true, for example, that while change in the price level is capable of inducing change in the quantity of money and (or) its velocity of circulation, yet as a matter of fact things regularly happen the other way? I am deeply suspicious of the conclusiveness of historical evidence in a matter of this sort, but, in any case, a good deal of factual investigation along this line, especially since the War, shows that that has not always been the sequence of events. Failing an historical justification, then, what explanation is there of the long and widespread acceptance of the Quantity Theory of Money as a "scientific" doctrine? Is it that writers on these topics were always pre-occupied in reality with questions of monetary policy, especially inflation; that they disapproved of inflation; disapproved of budget deficits and the sort of redistribution of wealth and income which inflation involves (I refrain from saying they were generally out and out defenders of the *status quo*); and that they formulated a "scientific" doctrine, without, of course, any deliberate intent to deceive, which would serve as a bulwark (though often, alas! a very frail one) against policies in which they disbelieved?

Mr. Keynes's views on this matter are, as always, of high interest. He understands perfectly that equations of exchange do not prove anything but are "mere identities; truisms which tell us nothing in themselves".¹ He believes, however, that his own equations bring together the factors that are significant in monetary problems and become valuable when "vitalized by the introduction of extraneous facts from the outside world".² This fact turns out to be the familiar one that in a capitalistic economy industry is guided by profit.³ But is not profit the result of other things? The result, for instance, of price relationships? Does the whole analysis boil down to this, then, that Mr. Keynes is of the opinion that, *for practical purposes*, if we want to control this particular complex of economic phenomena it will be more useful to seize upon, and work upon, the profit element than on anything else? There are passages in the *Treatise* which seem to me to state, or at least imply, this.⁴ But the reasons upon

¹*A Treatise on Money* (London, 1930), vol. I, p. 138.

²*Ibid.*, vol. I, p. 138.

³"The essential characteristic of the entity which we call Profits is that its having a zero value is the usual condition in the actual economic world of to-day for the equilibrium of the purchasing power of money. It is the introduction of this *fact* from the real world which gives significance to the particular Fundamental Equations which we have selected and saves them from the character of being mere identities" (*ibid.*, vol. I, p. 156).

⁴*E.g.*, *ibid.*, vol. I, pp. 168-70, 183.

which this practical judgment rests are not given in the *Treatise*. Perhaps they cannot very well be given there, but rest upon a multitude of personal observations and valuations which scarcely lend themselves to description. But if this is so, is monetary science a body of independent truth to which practice can look for guidance and to which, if it is to be sound, it must conform, or is it itself a body of doctrine built up to support a particular practical conclusion?

The case of what is often called "circular reasoning" illustrates, in a more general way, what I have been saying. If it is true as a general rule that all economic factors interact, how is one to escape from circular reasoning except through the door of purpose, or something like it? And this raises the still more general question of the proper function of economic science, or at all events of economic theory. Should it confine itself to the study of relationships and have nothing to say, directly, about questions of policy? That would not mean that it had no practical value, because a knowledge of relationships has a value of that sort in showing, for example, the implications of making a certain change in this or that element of an economic complex. That kind of economic theory would have the same sort of value for economic practice as mathematics has for engineering. But practical questions involve valuations and judgments as to expediency which may be regarded as belonging rather to the domain of Adam Smith's "insidious and crafty animal" than to the domain of science. This, it would seem, is the view of economic theory taken by the mathematical economists, and it has many attractions from the purely intellectual standpoint. Logical consistency may, however, as Marshall reminds us, be purchased too dear.

I suspect that questions of this nature lie at the root of the controversy about "real costs". Alfred Marshall was one of the clearest and deepest thinkers ever to write on the subject of economics, and he had an almost painfully high standard of intellectual integrity. But he himself said, in 1893, in his evidence before the Royal Commission on the Aged Poor that "I have devoted myself for the last twenty-five years to the problem of poverty, and very little of my work has been devoted to any inquiry which does not bear on that".⁵ And Mr. J. M. Keynes in his fine memoir of his great teacher has offered the gentle criticism that "Marshall was too anxious to do good".⁶ Have we got in this the fundamental explanation of those doctrines involving "real costs" and "consumer's surplus" which have been, not altogether unjustly, the target of so much criticism?

All this may seem to be far removed from the subject with which this

⁵J. M. Keynes (ed.), *Official Papers by Alfred Marshall* (London, 1926), p. 205.

⁶A. C. Pigou (ed.), *Memorials of Alfred Marshall* (London, 1925), p. 37.

article began. Doubtless there are differences, and not unimportant ones either, between the moulding of economic science by official compulsion on the one hand, so as to make it conform to and support a particular political conception and a particular line of policy, and on the other hand the same process in the mind of an individual thinker, even if he cannot quite be described as "free". Yet there is the fundamental similarity that in both cases economic thought is being fashioned into conformity with purposive ideas about what should be done in the practical world. Science is being made to follow practice instead of lead it. The Socialists long ago charged economists with being mere mouthpieces of the vested interests, which is the same as saying the advocates of capitalist policies. We have also been accused, quite recently, in fact, by a prominent man in this country, with being over critical of the established order. Both these things cannot be true, and the profession may, perhaps, take some comfort from the confusion of its enemies. But it should not take too much. For the Socialists may be right, in a more fundamental sense than they themselves meant. If this were realized economists would be much more cautious than many of them are in proffering opinions, in the name of the science, on current questions of policy—when one depression will end or another begin, whether inflation would be a good thing, and how much of it, and so forth. Economists properly have something to say on all these questions but they frequently say too much. With this comment the present article may well be concluded.

W. RUSSELL MAXWELL

King's College,
Halifax.