REVIEWS

Anwar Shaikh, *Capitalism: Competition, Conflict, Crises*
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John Grahl

A NEW ECONOMICS

Since the financial crash of 2007–08, the state of mainstream economics—already faced with incipient revolt from students, economic commentators and, increasingly, economists themselves—has become an open scandal. The debacle itself was preceded by hubristic self-congratulations at the end of major macroeconomic instability, a Great Moderation attributed to the felicity of neoliberal 'reforms' and to the wisdom of central bankers. One sign of growing impatience with all of this was the widespread welcome received by Thomas Piketty's studies of inequality which, notwithstanding his overly simplistic explanations of it, make a telling contrast with reigning macroeconomic models of a 'dynamic, stochastic general equilibrium'—mostly mathematically sophisticated *Robinsonades* based on a single, 'representative' agent that are useless for exploration either of social inequalities or of that other prominent feature of the contemporary financial landscape, default. Another is the foundation of the Institute for New Economic Thinking whose nearly one thousand researchers include many of the most interesting and original minds in the discipline, spanning a political spectrum from the Marxist left to right of centre.

In this conjuncture, Anwar Shaikh's *Capitalism* offers the prospect of an intellectual renewal more comprehensive than any so far attempted. Both the range and the depth of his book, covering in detail mainstream and heterodox, micro- and macroeconomics, are without parallel in contemporary literature. Its ambition is not confined to a critique of prevailing

doctrines. Shaikh advances corrected or contrasting views, supported by statistical evidence, of each central problem with which he deals, to construct an alternative account of the workings of capitalism and recent economic developments, particularly in the United States.

Capitalism is divided into three parts. The first stakes out preliminary methodological observations; the second covers the microeconomics of the firm, of prices and competition; the third, building on the first two, analyses the macrodynamics—laws of motion—of this form of socio-economic organization. Central to Shaikh's enterprise is the combination of empirical and conceptual theses in the first section, where he argues that orthodox economics fails not because it is abstract but because its abstractions are of the wrong kind, hypostasizing a notion of equilibrium in which economic processes are seen as essentially orderly. The currently dominant, 'post-Keynesian' challenge to this orthodoxy, on the other hand, which 'emphasizes the inefficiencies, inequalities and imbalances generated by the system', sees most economic outcomes as contingent, neglecting the evidence of order within the disorder of capitalism—the 'turbulent' convergence of prices on costs, the anarchic but nevertheless rule-governed allocation of capital across industries, and the recurrence over time of recognizable patterns in the growth and fluctuations of the system as a whole. In seeking to capture more accurately this order amidst turbulence, Shaikh takes the 'classical' economists—above all Marx, but also Smith, Ricardo and such figures as James Steuart and Thomas Tooke—as models in their grasp of both the rule-governed and the unruly nature of a capitalist economy. For in his words, 'it is important to distinguish between the conventional notion of equilibrium as an achieved state and the classical notion of equilibrium as a gravitational process.' He labels himself and most other theorists with a similar outlook as 'classical economists', although it seems likely that most of these colleagues would characterize themselves as Marxist, which he does not.

A key prop of Shaikh's construction is his dissenting view of aggregation. Whereas conventional economists use the notion of a representative agent to join micro- and macroeconomic planes, he insists on the difference between the two. Some factors of great importance at the level of the individual worker or enterprise cease to be so at the aggregate level. For individual cases are always heterogeneous, and the distribution of economic variables across them ensures that the whole is not the sum of the parts—there are emergent properties as one moves to the aggregate level. Criticizing the current fixation on micro-foundations, Shaikh argues that the same aggregate relation may often be compatible with several different explanations of individual behaviour, a point he illustrates with the example of a standard market relationship, a downward-sloping demand curve where a reduction

in price leads to an increase in demand. He uses the same example to show that there is no need to postulate any 'hyper-rationality'—full understanding of the economy as a whole, accurate anticipation of future developments, successful optimization in decision-making—to derive basic economic results. One consequence is a rejection of the 'analytical Marxism' associated with Gerry Cohen and John Roemer that accords explanatory primacy to the individual agent; but there is practically no significant development in economic theory over the last two centuries that escapes his survey of different doctrines, debates and schools of thought.

The final chapter in the first part of the book introduces Shaikh's view of capital, profits and prices. The driving force of the capitalist economy, governing both supply and demand, is profit, and the source of profit is surplus labour. However, the rate of profit does not depend on the quantity of surplus labour alone—it is affected by changes in relative prices determined by the (always 'turbulent') equalization of rates of profit across sectors with different ratios of capital intensity. This is the classic 'transformation problem', addressed because Shaikh uses 'prices of production' as the central points around which market prices gravitate, although of course the prices of production are themselves always fluctuating because of technical change and other forces. He interprets the difference between 'direct prices'—those corresponding only to the labour time necessary to produce each good or service—and 'transformed prices'—those where goods produced by more capital-intensive methods have higher prices, equalizing the rate of profit across the economy—as the result of a kind of transfer of value. The transfer takes place between the 'circuit of capital', which includes the flow of profits, and the 'circuit of revenue', which concerns only the payment of wages and purchase by workers of consumer goods. One could think of this transfer as the flow of investment away from capital-intensive sectors until prices in them have risen relative to those elsewhere, so equalizing rates of return.

In a survey of the whole literature bearing on this question, Shaikh rejects the recently influential approach to it by Duncan Foley and Gérard Duménil as no more than an accounting device. He also provides empirical evidence that, as suggested by Ricardo, the quantitative departure of prices of production from direct prices is limited, so that taking the transformation into account does not add much explanatory power to the simple labour theory of value (the Chicago economist George Stigler used to refer ironically to Ricardo's '93 per cent labour theory of value'). It must be said that it's not clear why Shaikh, or indeed other Marxists, regard this issue as so important. Apart from the question of relative prices, there do not seem to be any propositions in Marxist economics in general or in Shaikh's own version which depend upon it. It was Eduard Bernstein who suggested that the labour theory of value projected relations which are completely valid for

the capitalist economy as a whole onto microeconomic relations which are in fact differentiated according to capital intensity. A century of obsessive theoretical analysis has hardly disturbed this judgement. Shaikh's preliminary analysis further includes definitions of capital and profit, and the development of empirical measures of both, with impressive expertise and scholarship. He also argues convincingly that 'classical' concepts correspond more closely to standard accounting practices—notably in the treatment of profit margins—than do those of neoclassical economics, indicating the greater realism of the former.

The second part of *Capitalism* sets out Shaikh's microeconomics in the form of a theory of 'real competition'—which is 'antagonistic by nature and turbulent in operation . . . as different from so-called perfect competition as war is from ballet'—and a fully elaborated, and empirically supported, alternative to both standard price theory and the standard theory of the firm. The 'law of one price', linked to market equilibrium as an achieved state, gives way to the 'law of correlated prices' in a never-complete process of competitive equilibration around gravitational attractors which themselves are in motion. Although it is anarchic, real competition is rule-bound. From Ricardo and Marx, Shaikh develops a notion of 'regulating capital'. In each industry, this is the capital with 'the best generally reproducible conditions of production', that with lowest costs can attack the market share of other capitals in the same sector. That will not bring about full price convergence, but will force their prices down. As this happens, price equalization drives profit rates apart, since older or less efficient production units suffer a decline in profitability. 'Reproducible' conditions of production, however—that is, conditions not dependent on factors like particularly fertile land or exceptionally rich mineral deposits—turn the regulating capital itself into a target, as the industry it dominates attracts invasion by newcomers using technical advances to undercut its prevalent cost structure, in the pursuit of profit which motivates the system as a whole. Success in such invasion will not be a matter of marginal differences in cost. Its risks and difficulties require the cost advantages of the incomer to be 'robust'.

The rate of profit relevant to the real competition process is thus not the ratio of aggregate profit to the aggregate value of capital stock because the profitability of older and less efficient vintages of capital equipment, suffering gradual or drastic elimination, has no regulating force. What matters is the profitability of the latest capital investments—Shaikh uses as a proxy the 'incremental' rate of profit, or ratio of the change in aggregate profits to the level of new investments. In his view, aggressive new cost-cutting investment will take place even if the necessary capital commitments lower the achieved rate of profit. Today this is perhaps a controversial position in

Marxist political economy, since it lends credence to the notion that the rate of profit tends to fall as the organic composition of capital rises.

Both neoclassical and post-Keynesian theories postulate massive 'imperfections' in the competitive process. The neoclassicals cannot point to anything in actual economic processes corresponding to the notion of atomistic Walrasian competition where a host of identical enterprises adjust passively to price and cost changes over which they have no control. Hence, to begin to address observed realities they have to invoke various barriers to competition, failures of information and so on. Milton Friedman's attempted escape from this dilemma—the 'pragmatic' argument that the theory of perfect competition can be valid even if its basic assumptions are falsified—is dismissed by Shaikh on the grounds that the predictions of any theory must include its premises. Post-Keynesian theory, at least in the versions derived from Kalecki, also appeals to failures of competition in its account of price formation: distributions of income between wages and profits are derived from monopoly mark-ups, whereas Shaikh sees a conflictual struggle over wages, and the length and intensity of the working day as the starting point of their explanation. He provides striking statistical evidence that an (eventual, approximate, turbulent) equalization of profitability takes place across most industries, including those dominated by giant companies which might be thought exempt from competitive pressure.

Three further chapters complete the microeconomic side of *Capitalism*. The first argues that while the financial sector is subject to the same competitive process as other industries, its output price, centred on a 'price of production', is the interest rate, creating a gap between interest rates and profit rates which incentivizes investment. The second offers a long critical survey of debates on competition, displaying once again Shaikh's historical scholarship. A final brief chapter sketches an extension of his model of real competition to the international plane. Overall, it can be said that Shaikh's reconstruction of microeconomic theory ironically moves it closer to the teaching of business schools, where discussion focusses on tactical and strategic responses to real competitive pressures and opportunities—if always from the point of view of corporations. The much more critical implications of his models could, by contrast, be a formidable weapon in the struggle against the obscurantist and apologetic doctrines that dominate mainstream economics.

The final part of *Capitalism* builds out of these considerations an account of the macrodynamics of the capitalist economy. The emergence in the 1970s of the alarming phenomenon of stagflation, putting an end to any Keynesian consensus, led to a drastic tightening of monetary policy that undermined the position of labour and the welfare institutions of the

post-war decades. Academic economics, however, confined itself thereafter to the abstractions of general equilibrium; as Shaikh remarks, 'evidently one should not let reality get in the way of rigour.' Shaikh accepts Keynes's main insights into aggregate demand and liquidity preference, and seeks to integrate these into 'classical' theory, but differs from post-Keynesians on some key issues. The most important of these is his view that the cumulative or 'multiplier' effects of fluctuations in aggregate demand are smaller than is often supposed, because the savings ratio (inversely related to the multiplier) tends to vary in accord with investment spending, buffering the impact of the latter on economic activity, due to the simple fact that the corporations undertaking investment are also responsible for a large proportion of savings. For Shaikh, profit is at the centre of both macro- and microeconomics: 'Capitalist growth is regulated by the net profitability of accumulation enhanced through injections of purchasing power . . . But debt is the counterpart of credit, and debt-financed expenditures have limits even though modern credit and fiat money systems can postpone them for a long time.'

Shaikh takes his starting point for the macroeconomics of labour markets from Richard Goodwin's business-cycle model, a brilliant adaptation of the Lotka-Volterra equations originally developed for the biological interaction between predator and prey populations. The analogy makes unemployed workers the prey and profit-seeking capitals the predators. When predation is too successful, the decline in the available prey reacts on the predators whose own numbers decline, allowing the prey population to recover; in Marxian terms the effect of slower accumulation is to reproduce the reserve army of unemployed. This macroeconomic mechanism dominates the microeconomics of individual employment relations and justifies the insistence by Marx and Keynes that unemployment in the capitalist economy is essentially involuntary 'and obtains from (real) competition itself, not from restrictions on or imperfections in so-called perfect competition'. Shaikh extends Goodwin to include aggregate demand effects and a wider range of variables, in particular capacity utilization. He also measures the pressure of unemployment on the wage bargain not simply by the number of jobless but with an index that takes into account both the level and the duration of unemployment.

Turning to money and inflation, Shaikh addresses the recently influential 'Chartalist' theory of money, advanced in particular by Randall Wray. If the central bank and the government are treated as a single unit then the budget constraint on state expenditure is radically transformed. It no longer makes sense to maintain that government spending is limited by tax revenues. The 'Modern Theory of Money' uses this consideration to

advocate a role for the state as employer of last resort. Shaikh argues that neo-Chartalism rests on a range of implausible assumptions. As against orthodox theories of inflation, which relate it to tight labour markets, he suggests that aggregate supply constraints are best represented by a narrowing gap between the actual rate of growth and the maximum rate which is given by the rate of profit. As the gap narrows, an increasing number of supply bottlenecks are encountered.

The notion of an over-accumulation of capital itself as the barrier to capitalist development is a defining characteristic of Marxist economic theory. Shaikh ties his account of cycles and major crises to declining profitability, relating short-run business cycles to the turbulent balancing of aggregate demand and supply through the accumulation and decumulation of inventories, as against a slower process whereby the stock of fixed capital is adapted to profitability. He interprets the structural crisis of the 1970s as the outcome of a trend increase in the capital intensity of production, explaining the slowdown, together with a narrower gap between actual and maximum growth rates, accounting for the inflation. In the boom ensuing with the turn to neoliberal policies, accumulation was based partly on a decline in the wage share, but critically on ever-lower interest rates that at first increased incentives to invest, but eventually led to financial collapse and a general crisis. Attracted to the idea of long waves and recurrent major crises, he suggests that the crisis of 2007 arrived on time, in what looks like an excessively quantitative approach, underestimating the importance of qualitative transformations of social practices within the capitalist economy.

Capitalism is undeniably in some respects a difficult book. Detailed presentation of arguments sometimes obscures their overall direction; also, Shaikh is an accomplished mathematical economist who deploys equation systems along with most of these expositions. Those systems are complex in part because he usually wishes to distinguish actual from normal values of the key variables and to recognize feedback effects, such as the stimulus which rising labour costs give to the search for labour-saving innovations. An appendix lists some three hundred algebraic symbols. This condensed representation of his theories makes for slower reading. A second unavoidable limitation is that this is a critical study of economics as a discipline, and of the capitalist economy, whose scope and detail, but also careful empirical support for alternative positions, leave little room for considerations beyond the economic: almost nothing is said about politics or the state. But this is an outstanding achievement, based on decades of study and on a determination to subject every aspect of a vast domain to detailed examination (another aspect of which, not touched on here, is a meticulous critique of standard statistical sources). Shaikh's theory of actual competition offers a convincing

challenge to the 'idealizing abstractions' which prevail in mainstream doctrines, while the renewal of 'classical' macrodynamics points away from the empty scholasticism of 'general equilibrium' towards the realities of current capitalist development.

The scope and scale of *Capitalism* are such as to invite comparison with Marx's *Capital* itself, and it is a measure of Shaikh's accomplishment that it appears by no means absurd to apply that standard. Obviously we have here only a critique of political economy, without the revolutionary social and historical perspective of *Capital*, but the critique of doctrines is as thorough, detailed and accurate as that of Marx—perhaps exceeding it in generosity towards all economic theorists, of whatever school, who are seen as having made a genuine contribution to the understanding of capitalist relations of production. In the theories and interpretations that Shaikh himself advances, the main weakness is perhaps an excessive fidelity to his classical models, which leads him to neglect of the question of *periodization*—that is, of the successive transformations of the capitalist economy explored by such thinkers as Lenin or Luxemburg. Although this *magnum opus* reports the immense human costs of capitalist crisis, its ambition is essentially analytical—to promote a recognition of the systematic aspects of capitalism and the capacity for self-correction, which render it such a formidable antagonist.