A Common Misconception about Capitalism*

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There is a commonly-held view that while capitalism in its early stages brings about unemployment and hence an accentuation of poverty, this initial damage is subsequently reversed as it keeps growing. The unemployed get largely absorbed into the ranks of the active army of workers, and with a reduction in the unemployment rate, wages begin to rise; and they rise impressively as labour productivity increases.

This view appears at first sight to be supported by historical evidence: poverty in Britain is estimated by Marxist historian Eric Hobsbawm to have increased with the onset of industrial capitalism; but certainly from the middle of the nineteenth century things changed for the better as far as the workers were concerned. This would suggest that capitalism, no matter what transitional hardships it may cause to the workers, is eventually beneficial even for them.

This entire conception however is erroneous. There is absolutely no theoretical reason to expect that capitalism would reverse the damage it causes initially to the material conditions of the workers; and the reason for the actually-observed improvement in these conditions at a later stage has nothing to do with any spontaneous tendency of capitalism.

This idea that while capitalism may initially hurt the workers it later improves their condition, can be traced to the English economist David Ricardo, who had put forward the argument in the context of the introduction of machinery. He argued that such introduction initially displaces workers causing much hardship, but it raises the rate of profit and hence the rate of accumulation of capital, because of which the displaced workers are re-absorbed into employment; in fact the workers as a whole can even see an improvement in their wages if they do not reproduce themselves too rapidly and thereby control the rate of growth of the workforce.

Ricardo's argument has two obvious flaws. First, he was talking about a one-shot introduction of machinery; but capitalism introduces newer machinery and methods of production on a continuous basis. Even if we accept his argument that the unemployment-creating effect of a one-shot introduction of machinery would get reversed eventually through an enhanced rate of accumulation of capital and hence an enhanced rate of growth of labour demand, this eventual occurrence never materialises, as in the interim new rounds of machines are introduced.

The matter therefore has to be looked at in dynamic terms. If g is the rate of growth of the capital stock and also of output (the ratio of output to capital stock is assumed to remain unchanged despite technical progress whose main effect is supposed to be a reduction in labour cost) and p the rate of growth of labour productivity, then the rate of growth of labour demand is $g-p$. If this is less than the natural rate of growth of the workforce n, then the unemployment rate will keep on increasing over time. There is nothing in the working of capitalism to make $g-p$ exceed n.

Of course some would argue in defence of Ricardo that if labour productivity kept growing while the unemployment rate too kept increasing (so that the wage-rate remained tied to a subsistence level), then the rate of profit that could be obtained from production will keep rising and that this would keep pushing up the rate of accumulation until the unemployment rate fell significantly. But this is where the second problem with Ricardo's argument comes in, namely that he assumes that there would never be a demand constraint upon the realisation of the potential output and hence upon the rate of profit and the rate of accumulation. He assumes in other words that Say's Law, which asserts that "supply creates its own demand," invariably holds. But once we recognise that there is a "realisation problem", that the rate of profit, which emerges from the wage rate, given the conditions of production, need not be "realised", and that the rate of accumulation of capital stock, and with it the rate of growth of labour demand, need not keep increasing without limit, then it becomes clear that there is no mechanism within capitalism to reabsorb into the active army of workers all those who are displaced by its continuous introduction of technical progress.

Both the above points had been made by Marx in criticism of Ricardo's assertion that the introduction of machinery only had a transient ill-effect on the level of employment and the condition of workers. Once these points are taken into account, there is absolutely no theoretical basis for the belief that capitalism, while initially harmful to employment and the workers' condition, eventually improves their lot.

How then does one explain the indubitable historical fact that there was a turnaround in the living conditions of metropolitan workers in the course of the development of capitalism? The answer here lies in the large-scale emigration of European workers to the "New World" that occurred in the course of what is called the "long nineteenth century" (that is, the period up to the First World War). Between the end of the Napoleonic war and the First World War, according to economist W Arthur Lewis, approximately fifty million European workers migrated from their countries of origin to other temperate regions of white settlement, such as the United States, Canada, Australia, New Zealand and South Africa.

This was a "high wage" migration, since the wages both in their countries of origin and in their countries of destination, were high, in contrast to another wave of migration that was occurring simultaneously. This second wave was from tropical and semi-tropical countries like India and China to other tropical and semi-tropical countries like Fiji, Mauritius, the West Indies, East Africa and South-Western United States; these tropical migrants who were part of a low-wage migration were not allowed to move freely to the temperate regions of white settlement (they still are not to this day).

Lewis explains this difference between the high wage and low wage migration streams, by suggesting that there had been an agricultural revolution in Britain (which had spread elsewhere) that had raised the incomes of the rural population in their countries of origin. But there is very little evidence of any such agricultural revolution. The real reason for the high wages associated with the first migration was that the migrants simply took over the land belonging to the indigenous tribal population by force, and set themselves up as farmers earning high levels of income, which raised the wage rate both in the countries from which they came and the countries to which they came.

The scale of this temperate-to-temperate migration was very large: for Britain for instance it has been estimated that between 1820 and 1915, roughly half of the increase in population every year just emigrated. This in terms of scale would be analogous to roughly 500 million persons emigrating out of India in the period since independence. The possibility of migration on such a scale is just not available to persons in the third world today. But it is this possibility being available to the population of the metropolis that accounts for the turnaround in the fortunes of the European workers in the nineteenth century. It is not the spontaneous tendencies of capitalism that explain such a turnaround, but the fact that a large segment of the population could simply migrate abroad and by grabbing hold of the lands of the original inhabitants, set themselves up as reasonably well-off farmers. The possibility of snatching away land from the original inhabitants arose because of the phenomenon of imperialism.

Imperialism helped this process of a turnaround in the metropolitan workers' material conditions of life in a second way too. I mentioned above that the system being demand-constrained prevents the re-absorption of the workers displaced by machinery. But a demand constraint can be broken by selling machine-made goods at the expense of the artisan producers in the colonies and semi-colonies, as indeed happened historically. This would have the effect of reducing or keeping low the level of unemployment in the metropolis; indeed it would amount de facto to an export of unemployment from the metropolis to the colonies and semi-colonies, who are powerless to protect their economies from such deindustrialising imports because they are ruled by the metropolis.

It follows that contrary to the misconception that capitalism itself tends to overcome the initial damage it inflicts on the working population of the metropolis, it is the phenomenon of imperialism, which ensures both a land grab around the globe and an export of unemployment to the colonies and semi-colonies, that underlies the turnaround in the fortunes of its domestic workers. This must not be taken to mean that the workers in the metropolis are complicit in the imperialist project; it is just the way the system works.

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