

The Limits of Capitalism

The following is a lecture I gave on the limits of capitalism to our class at our church's Servant Leadership School that was a conversation between the Gospel and capitalism. It's a beginning look at some of the inherent limitations of capitalism in dealing with some of our most important problems.

One of our primary objectives during this conversation between capitalism and the Gospel is to begin a discussion on the limits of laissez-faire, free-market capitalism, so that we can begin to define alternatives that will better serve God's creation. I'd like to suggest that the current global economic structure cannot—even in theory—deal adequately with the primary problems facing humanity today. Regardless of our politics, unless the economic system changes significantly, our civilization will not survive.

What I want to do in the next few minutes is to lay out a simplified outline of the basic structure of free-market capitalism, describe why our major economic problems can't be solved within that structure (as opposed to alternate varieties of capitalism that exist elsewhere), and briefly suggest some straightforward modifications of free-market capitalism that would move us toward a more just, more sustainable planet.

There are at least three bedrock conceptual foundations of capitalism: private property, free markets, and self-interest as the basis on which people act.

1. An essential characteristic of capitalism is that the means of production are privately owned, so "private property" is central. In the European tradition, John Locke posited private property as a "natural right." And in the American tradition, the inviolability of private property has been legally almost absolute. Unless it's expressly illegal, I can do anything I want with what I own, including refusing to offer what I have for whatever reason I want or for no reason at all, so private property gives owners (in the collective) the right to refuse others access to livelihood.

2. There have always been "markets," but the unconstrained, laissez-faire, free-market that is the American ideal means that all goods and services are bought and sold purely on the basis of price, and that includes labor. Laissez-faire is a French expression that means

non-interference in the affairs of others; in economics it refers explicitly to government non-interference in the markets.

A. Having described free markets, however, it's important to recognize, however, that they don't really exist. Markets always exist within, and are influenced by, social frameworks. There's never been a true laissez-faire economics unshaped by social and political realities, primarily because the fall-out from such an economics leads to political backlash. So, why am I talking about it? Well, we need to understand it, anyway, because—especially in American discourse—the “free market” has become such a sacrosanct ideal that it's a very powerful club for diverting any debate about how to deal with basic social issues, even internal debate within ourselves. So we need to be armed with an understanding of it and its limitations.

B. To understand the function of the market in economics, it's helpful to think of it as an information network and prices as the messages that can coordinate incredibly complex processes of production very efficiently. Prices replace value decisions.

C. For the market to work efficiently, however, at least two other conditions must be met:

- 1) First, there need to be many buyers and many sellers (so that the sellers have to compete with other sellers and buyers have to compete with other buyers to get the best and cheapest product).
- 2) Second, information flow within the society must be unhindered so that everyone knows what's available for what price.

3. Adam Smith, an eighteenth century English philosopher and economist, recognized that the market would operate most efficiently if all buyers and sellers operated purely on the basis of self-interest to maximize their own benefit. If each person bought and sold (including one's labor) in order to maximize his own personal profit, Smith believed that the laws of supply and demand would establish prices that maximized production. Smith was writing in the late 18th century, when economists still believed that their role was to direct the economy so that the whole of human society benefited. But he believed that in the free market and its pricing mechanism he had discovered a natural, God-given law that would allow everyone to prosper—as if by an “invisible hand”—if each person worked solely for his own benefit. “[B]y listening to the voice of self-interest and obeying the dictates of the free market,” Smith wrote, “we benefit the poor just as if the earth had been ‘divided into equal portions among all its inhabitants.’” (p. 46 in *Beyond Poverty and Affluence*) Modern, free-market economists still believe in some version of that, which means that they don't have to concern themselves with the just distribution of goods leaving it to the market instead.

Those are the building blocks of capitalism.

Before looking at some of the problems inherent in capitalism, we have to allow that an economics that approaches laissez-faire, free-market capitalism is—at least in the short term—by far the most efficient economic system devised. If one measures only economic output defined in dollar amounts, capitalism swamps other forms of economics.

Let's take a look at some of the essential problems in how this works out.

1. First, there's the question of "externalities." Since one of the primary parameters of competition is price, reducing the cost of a product is essential to stay competitive, but because everything is measured in prices, the producer is concerned with her own dollar costs. So, any "cost" of production that can be shoved out somewhere else (or "externalized") no longer really counts in the economic equation for the producer. If I can spew pollutants and carbon dioxide into the air, for instance, it doesn't cost me anything, so I've "externalized" onto society all the cost of cleaning up my waste products. These are "negative" externalities. There are at least two problems here.

A. First, the cost of the product to the buyer doesn't really reflect the true cost of the product, so lots of people who don't benefit from the product end up paying for it.

B. Second, because the costs of removing the pollutants from production is not a cost to the producer, there's no way for it to enter into the economic equation, which leaves no incentive to minimize the cost, even if that cost would be very small compared to the ultimate cost of clean-up.

In the real world, of course, we could force polluters to capture those externalized costs by making them pay taxes equivalent to what it costs to clean them up, but within free-market, laissez-faire capitalism itself, there's no virtually no mechanism to curb the environmental costs of production.

Harold Stone has also pointed out to me that the economic equation also doesn't take into account "positive externalities," further distorting accurate valuation within the system. For instance, offering high quality primary and secondary school education benefits the recipient, but it also benefits future employers, the government (in terms of higher taxes), and most importantly society in general. But there's no way to put the benefit to those other entities into the usual economic model, so education is economically undervalued ... and consequently underfunded.

2. One specific form of negative externalization results from the fact that the true value of currently abundant but naturally limited resources is not reflected in the cost to the producer.

When oil is abundant it's cheap, despite the fact that it's being used up and can't be replaced. So the real value of that resource to future generations simply can't come into the equation. One can already imagine a time when oil will be too expensive for most people to afford, but their needs can't be priced into capitalism's price system now. This is a form of externalization of costs onto future generations. 3. Capitalism always leads to economic inequality, and the more laissez-faire the system is, the greater the extremes of inequality. There are several reasons for this inevitability.

A. Even if all other things are equal, of course, people have different abilities and are more or less able to handle the complexities of competition, so fortunes differ markedly.

B. More practically, all other things aren't equal, specifically everyone doesn't start out equal, so country of birth, inherited wealth, levels of education, connections to powerful people, racism, and so on give some people extraordinary advantages over others.

C. Moreover, within capitalism most people become wage-earners working for others who own the means of production. Marx and others have called this "wage-slavery" because labor becomes a "property" that one "sells" to the capitalist, so for practical purposes one is owned by the capitalist while working. There are several problems here.

1) Most obviously, since the capitalist owns the means of production, all of the profit belongs to her ... and not to the workers. The assumption here is that it's the capital that has produced the profit (contrary to Marx, for instance, who credited labor with producing what's called the "surplus value" or profit). Within the capitalist assumption, labor is just another means of production, like a raw material, that has been purchased.

2) Another reality is that the competition of the market and the desire for maximum profits pressures the owners (or managers) to reduce costs to the minimum, which means that the cost of labor should be minimized, which means that the owner is always trying to keep wages as low as possible. Adam Smith believed that since there would always be many small producers, individual workers could force them to compete for laboring services, ensuring fair wages. Smith explicitly ruled out international trade and didn't foresee the huge companies and surplus labor produced by current economic policies. The billions belonging to the Walton family and the minimum wages of Wal-Mart workers is the inevitable result.

D. People who have nothing to sell can't take part in the market. Many disabled individuals and children can't take part in the market at all, while many more partially disabled people, single parents, unskilled workers, uneducated people, or people in countries with no functioning infrastructure can't sell their labor for a price that will allow them a real livelihood. To the extent that all economic activity within capitalism takes place in the market, then, there are hundreds of millions of people who can take part only to a very limited extent, leaving them destitute.

E. Finally, within capitalism itself there is no concept of justice or fairness. That is supposed to be taken care of by Adam Smith's "invisible hand," so any individual owner or stockholder or manager isn't doesn't need to concern himself with the unfairness of the system. It is no exaggeration to say that pure capitalism is simply incapable of dealing with the world's poverty and destitution.

4. Because price is the only kind of information that capitalism can work with, human needs and wants can't be accurately valued. Dog food for the wealthy is more valued than subsistence sustenance for starving human beings because the wealthy can pay more. There's no accountability within capitalism for serving human needs.

5. We've talked about some of what happens when labor becomes merely another factor of production. There are other consequences:

A. Certain kinds of work that are extraordinarily valuable to society have no value within capitalism. Women caring for children and the household at home have no economic value ... unless they go to work and hire someone to take their place, which leads to the bizarre condition that when a spouse leaves home and goes to work and hires a nanny, the "value" increase to the economy is two-fold, while the actual value to society of having parents away from home all day long may very well be negative. Teachers are, perhaps, the most important professionals in our society, yet it's difficult to assign a price tag to their work so they are decidedly underpaid in an open market.

B. Because labor is a cost, it has a negative value. So, the intrinsic value of work disappears from the economic calculation. Work is only instrumental. But in reality, the quality of our work has a high human value. Like the environment, if work is treated only instrumentally, then we can have huge human losses that are not registered.

6. As begins to become obvious, within capitalism itself, there's no way the society can think about how we can become prosperous together. Capitalism is inherently individualistic and has no way of measuring societal well-being except through gross national product. Adam Smith and the classical economists believed that the invisible hand would do this automatically. For modern-day apologists, the solution to human destitution is to produce more goods, and let the market worry about distribution. As we've seen, however, the market's distribution is not inherently just. More importantly, environmental conditions simply won't allow for continued expansion of the economy. The only solution (Produce more so that it can trickle down to the poor) is no longer possible ... if it ever was.

7. And that is the final, and perhaps most difficult problem. Capitalism depends for its survival on constant growth. It must continue to sell us more and more. Yet it becomes more and more clear that we must, in fact, consume less and less if we're all to survive. Capitalism cannot comprehend that problem, much less solve it. The conclusion is that the major problems that humanity faces are all wrapped up in the economic system, and laissez-faire, free-market capitalism is incapable, theoretically and practically, of dealing with them.

There are, however, relatively straightforward theoretic (and practical) ways of dealing with the primary deficiencies. In practice these can turn out to be enormously complex and politically difficult to implement, but the direction we must go is, I think, obvious.

1. First, we need to compel producers to internalize the enormous costs that capitalism externalizes to society in general and to future generations. Capitalism by itself simply cannot do this. One obvious mechanism is governmental and inter-governmental taxation and regulation. Government imposed taxation can represent those externalized costs and collect them from the producer. Where costs are simply too great, industry needs to be regulated so that the process is abandoned. How these costs are determined and levied, of course, is not a simple matter, but the theory is clear.

2. Second, access to livelihood needs to be guaranteed to everyone. There are several different mechanisms.

A. To some extent, income needs to be redistributed so that no one is destitute. The Earned Income Tax Credit is an example of an effective program that partially redistributes income.

B. Second, the other basic resources necessary to access livelihood need to be provided to everyone:

- 1) Job training
- 2) Education
- 3) Health care
- 4) Childcare

3. Third, some kinds of care that are essential to society but not appropriately remunerated need to be subsidized by society: teachers, child-care workers, health care workers, and to an important degree parenting during early childhood.

Pure capitalism, again, can't do these things, but it's a natural function of the state, which we should encourage.

To summarize briefly, capitalism is inherently incapable of dealing with the extraordinary problems of externalization of costs onto society and inequality, but at least in theory government and inter-governmental bodies can deal with these problems and must.

There's another problem that must be mentioned, which I'm a bit more pessimistic about. I am not sure that a democratic government can decide on a reduction of consumption, especially of the magnitude necessary. Within capitalism, growth is an unmitigated good. But it's clear that consumption among the affluent needs to be limited if we are to survive. At the current state of spiritual development in our society, I'm not sure we're capable enough of desiring a limited consumption to enable legislating it. It is in this area that spirituality, and specifically, our little religious bodies might make great contributions.