Kalecki and Steindl in the Transition to *Monopoly Capital*

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Paul Baran and Paul Sweezy’s *Monopoly Capital* is a classic that has long outlived the conjuncture in American capitalism that it described. In a deep and scholarly way, its authors exposed the deep structure of that capitalism, which determined the dynamics of the system and therefore those “surface” phenomena of unemployment and poverty—symptoms not of any functional malaise in capitalism (the “market failures” beloved by academic economists), but of the very way in which modern capitalism works. The authors of the book may therefore be forgiven for providing only the lightest sketch of the ideas and theories they used in their analysis. In this essay, I try to uncover some of those ideas and theories to show how they represent a shift from the analysis in Sweezy’s earlier work the *Theory of Capitalist Development*, and how the two books are linked to the ideas of Karl Marx in a way that can only be understood through the work of Michał Kalecki and Josef Steindl. Baran and Sweezy knew and admired Kalecki and Steindl and, as I will try to show, continued what might be called Marx’s “project” very much in their spirit.

From Marx

The publication of the collected writings of Marx and Engels in various increasingly comprehensive editions made it fashionable among Marxists to scan his works to find quotations or doctrines congenial to their own outlooks or enthusiasms; or, among more scholarly readers, to find the “true” meaning of particular doctrines. This gave rise to splendid and wordy rhetoric, but poor analysis. Sweezy’s teacher Joseph Schumpeter had a point when he remarked that “The cold metal of economic theory is in Marx’s pages immersed in such a wealth of steaming phrases as to acquire a temperature not naturally its own.”¹ Such rhetoric focuses attention on doctrine and clichés rather than on understanding. It is probably the most common cause of sectarian division among Marxists, as well as of the papering over of problems in theory and practice. Political economy is not received economic wisdom, a set of doctrines that must

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be true simply because Marx said so or because it is necessary to have a theoretical starting point in any study of society.

To understand Marx, as with any other great thinker, it is necessary to understand not only the content of what he wrote, but also its structure. Only in the context of that structure is it possible to find out the meaning of particular observations. In other words, it is necessary to understand Marx’s project and, in this essay, how that project was continued by Baran and Sweezy. Marx’s project was to uncover how capitalist production and distribution determine the ways in which capitalism had evolved, combined with a systematic criticism of dominant economic ideas and policy. As is well known, Marx’s political economy is based on a theory of value and of the creation of value. Volume II of Capital, subtitled The Process of the Circulation of Capital, was supposed to show how value is realized. This process is what we now call the circular flow of income: the income flows that Marx described in the schemes of reproduction are laid out in this volume. However, he was not satisfied with the draft he had written and intended to revise it. In particular, he showed a scheme of simple reproduction (reproduction without any increase in production, or of the capital stock), but he did not complete the exposition of expanded reproduction.

Following the writing of Capital, a radical change occurred in the functioning of the capitalist economy, with the emergence and proliferation of markets for long-term debt and shares in capitalist enterprises. Legislation from the 1860s on eased the establishment of joint stock companies in the advanced capitalist countries, pioneered in Britain and the United States. This transformed capitalism from its “classic” form in the mid-nineteenth century, in which enterprises were owned and controlled by individual capitalists and their more or less active partners, into its modern, twentieth-century form, dominated by large joint-stock companies. Earlier joint-stock companies created to build canals and railways and to finance coal mines had required special legislation. (These early corporations were the subject of Paul Sweezy’s doctoral thesis Monopoly and Competition in the English Coal Trade, 1550–1850.)

The processes of centralization and concentration facilitated by this change had two consequences of radical importance for the stability of capitalism. In the first place, large capitalist enterprises with access to capital (long-term debt and equity) markets were able to fund their long-term industrial assets with bonds, or equity. This reduced their vulnerability to credit shortages. Before this change in financing, the classic capitalist enterprise was typically financed with the owner’s capital. But as mechanization of production proceeded, there was an incessant need
for additional capital that was usually met by short-term bank borrowing, which had to be rolled over during the lifetime of the productive capital equipment that it was financing. If banks became reluctant to lend, the capitalist entrepreneur (Marx’s “functioning” capitalist) would be unable to roll over outstanding short-term debt and, faced with a squeeze on liquidity, the company could fail. This is the financial crisis typical of classic capitalism. It was described in the text that formed the basis of the theory of financial crisis in both mainstream economics and radical political economy, Tugan-Baranovsky’s study of English banking crises, which accompanied his famous “solution” to the problem of the declining rate of profit by means of increasing the capital-intensity of production.

In his 1932 preface to the second edition of Hyndman’s Commercial Crises, the great liberal political economist John A. Hobson, who was to influence Lenin’s theory of imperialism, attributed the characteristics of nineteenth-century crises to those of the twentieth century, with under-consumptionist implications:

The interest of modern readers will be attracted by the common character of the nine crises of the last century, and by the flood of light they throw upon the present troubles of the world. Even in the slump which followed the Napoleonic war the germ of all the later slumps was plainly discernable, the glut of commodities unsaleable by reason of the fall of prices, the stoppage of production throughout the industrial system, and the lingering waste of unemployment. In each succeeding crisis, though financial troubles figured as the immediate cause of collapse, the same paradox which confronts the world to-day was plainly visible, an acceleration of the power of production unaccompanied by a corresponding growth of purchasing and consuming power.

The change in capitalist financing affected the organizational forms and structure of capitalist enterprises, the course of financial crisis, and capitalist dynamics in general. The emergence of long-term debt markets allowed the capitalist entrepreneur to refinance short-term bank borrowing with long-term bonds. For the capitalist with access to such long-term finance, such finance virtually eliminated any vulnerability to a bank credit squeeze. At the same time, the capitalist entrepreneur had to ensure that the company now had sufficient liquid reserves to make interest and dividend payments on long-term debts, or equity, and then to ensure that the holders of the bonds or shares were not embarrassed by the drying up of liquidity in the markets for bonds or shares. Such a drying up makes it difficult to sell a bond or share for a good price, and condemns its owner to holding it until prices improve, with only a cash flow in the form of interest or dividends. Hence companies
are obliged to hold excess capital that is turned over in restructuring their financing.

The second major change attendant upon the expansion of long-term finance was the rise of monopoly capital. Companies could now expand far more expeditiously by buying their competitors' long-term debts or shares, rather than entering into the precarious business of competing their competitors out of business. The trusts and monopolies that dominated capitalism by the end of the nineteenth century were the creation of the capital markets, rather than, as academics like Alfred Marshall believed, the results of either “natural” or political monopolies, or of increasing returns to scale.

Rudolf Hilferding recognized that the link with the capital markets forms the essence of monopoly capital. In his *Finance Capital*, Hilferding first put forward an explanation of a new kind of capitalist instability, caused by the interplay between monopoly and competitive segments in the capitalist economy: corporations could stabilize their finances through access to the capital market and the use of monopoly power and cartels to secure a disproportionately large share of the surplus generated in the economy. This meant that they were less inclined, in a recession, to eliminate the excess capacity whose scrapping was the precondition for an investment-led recovery. This prolonged economic depression, and forced the burden of adjustment in productive capacity onto the competitive sector of the economy. Hilferding anticipated that the capitalists in the competitive sector of the economy would naturally get fed up having economic crises dumped on them by the monopolists, and would eventually join cartels to secure some protection from economic instability.

**Kalecki and Steindl Join the Debate**

Hilferding’s conclusion that capitalism had now changed its mode of operation, its structure, and its dynamics was widely accepted by Marxists, even if many rejected his view that cartelization and the coordination of business activity could effectively stabilize the capitalist economy. Of Hilferding’s intellectual legacy, his theory of imperialism and his distinction between “classic” and “monopoly” capitalism were broadly accepted by Marxists such as Vladimir Lenin. The greatest controversy among Marxists was aroused by Hilferding’s hints that capitalism could be stabilized by the management of its markets. Among the Marxists of central Europe, the arguments around this idea overlapped with the debates over Rosa Luxemburg’s critique of Marxist orthodoxy, and the questions she raised about how surplus value is turned into money. On the one hand, Tugan-Baranovsky had sketched possibilities
of capitalist development with greater use of machinery—possibilities limited, as in Hilferding, by political contradictions. On the other hand, Henryk Grossman argued that capitalism was destined to collapse due to the inevitability of the decline in surplus. Paul Sweezy was to give a good and judicious summary of the issues in the chapter on the “breakdown controversy” in his first serious exposition of Marxist economics, *The Theory of Capitalist Development*.

But Sweezy did not take up all the themes that emerged from those discussions. Among the contributors was the German social democrat Emil Lederer, who in 1927 published a theory of the business cycle that can be seen as a direct criticism of Hilferding’s economic stabilization thesis. Lederer argued that monopolies and cartels tend to make business cycles more extreme, because those monopolies tend to over-invest in a boom and ensure that consumer prices will not fall in a recession by as much as wages (so that real wages will fall). He therefore attributed booms to investment, but regarded recessions and depressions as ultimately attributable to a lack of consumption demand. In regard to the boom, Lederer was clearly anticipating Kalecki. With regard to the recession, Lederer was still bound by the underconsumptionism that prevailed among the radical critics of capitalism, and that may be found in Marx and in Sweezy’s *Theory of Capitalist Development*.

Kalecki was unaware of Lederer’s theory of the business cycle. But the Polish economist readily joined in the critique of monopoly stabilization envisaged by Hilferding. The result was that Kalecki’s theory of the business cycle simultaneously resolved the problem that Rosa Luxemburg had found in Marx’s theory of capitalist reproduction—namely, how capitalists can realize their profits in money form—and anticipated Keynes’s analysis, showing how output and employment in a capitalist economy depends on the level of investment in that economy. What came out of Keynes’s *General Theory* was a striking theory of aggregate demand in a setting of long-term financing. What was missing, however, was any analysis of corporate finance that would reveal the place of finance capital (rather than abstracted “aggregate demand”) at the heart of modern capitalism, and the link with Marx’s analysis showing the necessity of investment in realizing profit.

Kalecki was later to observe that his theory was already “contained in the famous Marxian scheme of ‘extended reproduction.’” But in Volume II of *Capital*, the problems of the business cycle, he wrote,
investment and consumption goods industries, which is necessary in order to secure a steady expansion of output.... He does not pay attention to the problem of what happens if investment is inadequate to secure the moving equilibrium, and therefore does not approach the idea of the key position of investment in the determination of the level of total output and employment. Exactly the reverse attitude is represented by one of his eminent pupils, Rosa Luxemburg. In her Akkumulation des Kapitals she stressed the point that, if capitalists are saving, their profits can be “realized” only if a corresponding amount is spent by them on investment. She, however, considered impossible the persistence of net investment.... The theory cannot be accepted as a whole, but the necessity of covering the “gap of saving” by home investment or exports was outlined by her perhaps more clearly than anywhere else before the publication of Mr. Keynes’s General Theory.16

Kalecki therefore shifted the basis of inadequate aggregate demand from underconsumption, an obvious feature of poverty in all societies, to under-investment, which prevents the full realization of profit. He went further and tried to show that the crucial function in a capitalist economy of the price system is not simply to make supply equal to demand in markets—a commonplace from merchant capitalism—but lies in determining the distribution of profits among capitalist firms. It is through their manipulation of prices in markets that corporations or monopoly capitalists secure for themselves a disproportionate share of the profits realized through investment and trade in the economy. This again develops insights previously found in Hilferding and Marx.17 But it should be pointed out that monopoly is not the outcome of operations in markets for goods and services, where monopolists may happen to have a dominant position, but is instead the result of their operations in the capital market. The dominant corporations of today, such as General Electric, Tata, Boeing, or Microsoft, did not achieve their preeminence through their ability to produce electrical equipment, steel, aircraft, or software better than their competitors, but by buying up those competitors in the stock market.

This theoretical insight was taken up by Steindl, Kalecki’s friend, from the time when they worked together as anti-fascist exiles in Oxford during the Second World War. Steindl was later to recall:

On one occasion I talked with Kalecki about the crisis of capitalism. We both, as well as most socialists, took it for granted that capitalism was threatened by a crisis of existence, and we regarded the stagnation of the 1930s as a symptom of such a major crisis. But Kalecki found the reasons given by Marx, as to why such a crisis should develop, unconvincing; at the same time, he did not have an explanation of his own. “I still do not know,” he said, “why there should be a crisis of capitalism.” He added: “Could it have anything to do with monopoly?” He subsequently suggested
to me and to the Institute [of Statistics in Oxford, where they were working], before he left England, that I should work on this problem. 18

So began Steindl’s work on his most important book, *Maturity and Stagnation in American Capitalism*, which along with Kalecki’s *Theory of Economic Dynamics* was to have such a strong influence on Baran and Sweezy. As Steindl later observed, the question set by Kalecki “was a very Marxian problem, but my methods of dealing with it were Kaleckian.” 19 Stripped down to its fundamentals, Steindl’s *Maturity and Stagnation* argued that monopoly capital could use its control of markets to prevent the elimination of excess capacity in industry. In competitive capitalism, getting rid of excess capacity is the precondition of an economic recovery when firms’ investment restarts, if only to replace worn-out equipment. According to Steindl, corporations continue operating under excess capacity, covering the higher costs of that excess from their monopoly profits. However, the unused capacity discourages fixed investment in the economy, and hence maintains a regime of economic stagnation due to under-investment.

Kalecki and Steindl thus took on Marx’s project and developed it for the conditions of twentieth-century capitalism, building on the work of Luxemburg and Hilferding. Most of Kalecki’s and Steindl’s Marxist contemporaries reacted differently to those same conditions and events in the first half of the last century. The response to Keynes’s ideas in economic theory and policy was to point out that Keynes did not adhere to the labor theory of value, even if he recognized a problem of insufficient demand in the economy. This was then the pretext for what I have elsewhere called the Marxist retrogression to Ricardian socialism—that is, a regression to the fundamental principles of the radical political economists who had preceded Marx, writers such as John Gray (1799–1883) and Thomas Hodgskin (1787–1869). Those fundamental principles were the labor theory of value (from which the Ricardian socialists derived their case for socialism as the right of labor to its products) and underconsumption as the cause of poverty in capitalism, because workers were not paid the full value of their labor, and therefore could not buy all that they produced. While Marx had criticized the Ricardian socialists for their moral critique of capitalism and their inability to see the workings of the system as a whole, he shared their insistence on labor as the source of all value and recognized underconsumption as a symptom of capitalist depression. 20 The experience of the 1930s reinforced those elements in Marxist economic thinking. As Steindl was to observe of later developments in Marxism, which were also partly in reaction to Baran and Sweezy’s *Monopoly Capital*: 
Marxism and radical economics, grown mainly from the ranks of the student movement since about 1968, have come to oppose the mainstream.... This movement has not penetrated economics, rather it has established a ghetto. It has carved out a place for itself at the universities and has left the mainstream intact, and that mainly owing to the attitude of Marxists themselves, especially their lack of interest in current economic policy. The renaissance of Marx has concentrated not on emulation but on exege- sis of his work. No doubt very much has been achieved here and we can be grateful for it. But Marx lived very much in his time and the Marxist economists do not seem to follow his example.21

Monthly Review was an honorable exception to these developments in Marxism. The resort to underconsumption as the explanation for economic depression and stagnation by Marxists retrogressing to Ricardian socialism was merely a symptom of a much more fundamental rejection of any distinction between the classic capitalism that Marx described and the finance capitalism that had emerged after the 1870s. This is why many Marxists were caught unawares by the increasing prominence of finance in the early years of this century, and why the theories of “fi- nancialization” that emerged from this Marxist analysis combine classic capitalism with underconsumption, reinforced by a Ricardian view of debt in which debt is never an asset, as it is in a credit system, but merely a usurious claim on income. A much more sophisticated view of finance was presented by Kalecki and Steindl, and later Sweezy and Magdoff, precisely because they recognized the innovations in the capitalist firm that were noted by Hilferding in his Finance Capital.

The Transition to Monopoly Capital

In their introduction to Monopoly Capital, Baran and Sweezy presented their new book as “a direct continuation of our earlier work.”22 Two books in particular are mentioned: Paul Sweezy’s The Theory of Capitalist Development and Paul Baran’s The Political Economy of Growth. Sweezy had published the former in 1942, at a time when he knew the work of Keynes (whose General Theory he hailed as “undoubtedly the most important work by an English economist since Ricardo’s Principles” and marking “the emergence of Anglo-Saxon economics from roughly a century of sterility”).23 But he makes no mention of Kalecki. The analysis of capitalist depression given in this earlier book is fundamentally an underconsumptionist one. The tendency toward monopoly, Sweezy wrote, “lowers the rate of consumption” as wages and employment are squeezed, while investment is driven into the competitive sector where it returns a lower rate of profit: “Investment in monopolized industries is choked off; capital crowds into the more competitive areas. The rate of profit which is
relevant to investment decisions is therefore lowered. This is a factor in causing depressions independent of both the general falling tendency of the rate of profit and the tendency to underconsumption.”

Sweezy finally got to know the work of Kalecki when the latter arrived in New York at the end of 1946 to take up work at the United Nations. The two men met regularly through the nine years while Kalecki was in New York. The influence of their discussions on Baran and Sweezy is obvious. Baran’s book, published in 1957, cites Kalecki and Steindl, in an analysis that recognizes the role of investment in the realization of profit. In his introduction, Baran mentioned Kalecki, along with Charles Bettelheim, Maurice Dobb, Leo Huberman, Oskar Lange, and Joan Robinson, as “friends” who had discussed key ideas in the book with their author, and read all or parts of the manuscript.

In Monopoly Capital there is a shift of focus from Sweezy’s earlier book. The fundamental problem in capitalism, its tendency to stagnation, is no longer general underconsumption, because the workers are unable to spend the full value of their labor and because monopolies can force down real wage income, but instead the less obvious problem of the monetization of profit that Luxemburg identified and Kalecki clarified. In chapter 4 of Monopoly Capital, the authors clearly put forward the fundamental method by which capitalist “surplus” is “absorbed” (or monetized), namely through capitalists’ consumption and investment. The cause of stagnation lies in inadequate investment and the Veblenian “waste” of the sales effort, advertising, militarism, and bureaucracy. This shift in its authors’ analysis of capitalist stagnation they owed to their discussions with Kalecki and Steindl.

Monopoly Capital represents the convergence of Marxian political economy with the ideas that emerged in the wake of the development of that political economy by Luxemburg and Hilferding, ideas that would be accurately described as the Keynesian Revolution, if only Keynes had understood the impact of Luxemburg and Hilferding on economic theory. Kalecki’s critique of Luxemburg and his implicit critique of Hilferding laid not only the basis for Kalecki’s own contribution to the Keynesian Revolution, but also for Baran and Sweezy’s clearer understanding of capitalism and its limitations.

Notes

1. Joseph A. Schumpeter, Capitalism, Socialism and Democracy (London: Allen and Unwin, 1987), 21. Sweezy’s own work was effective precisely because he avoided steamy excess and was content to let the analysis and the facts speak for themselves.
just as advertising, product differentiation, artificial obsolescence, model changing, and all the other devices of the sales effort do in fact promote and increase sales, and thus act as indispensable props to the level of income and employment, so the entire apparatus of “finance, insurance, and real estate” is essential to the normal functioning of the corporate system and another no less indispensable prop to the level of income and employment. the prodigious volume of resources absorbed in all these activities does in fact constitute necessary costs of capitalist production. what should be crystal clear is that an economic system in which such costs are socially necessary has long ceased to be a socially necessary economic system.

— Paul A. Baran and Paul M. Sweezy, Monopoly Capital, 141