

**“Economics for Everyone:  
*How to Cut Through the Jargon*”**

Later Life Learning, Innis College

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Fall 2021

# Session 2

**A Little History**

**Readings:  
Chapters 3-4**

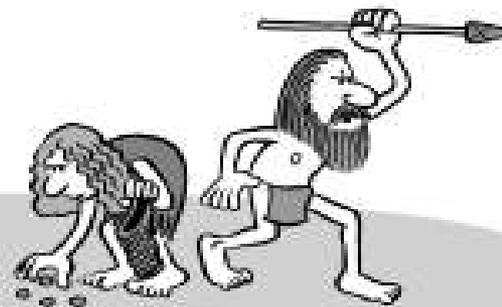
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Tony Biddle***

# The Economy is Always Changing

- The economy is constantly evolving:
  - What we produce
  - How we produce it (technology)
  - Our relationships to other people
- It's very important to study economic history
  - Provides perspective to today's capitalism
  - Proves that the status quo isn't permanent
- Economics is also in constant flux, changing alongside the economy

# A Short History of the Economy

- **Hunter-gatherer societies**
  - No surplus.
  - Very flat social structure.
- **Slavery**
  - Permanent agriculture allowed for a surplus to exist.
  - This opened a social conflict over who controls it.
  - Class divisions appear within society.
- **Feudalism**
  - A more sophisticated, subtle class structure.
  - Peasants did the work, landlords collected surplus.
- **Capitalism**
  - Social structures evolved to match the needs of new technology that produced much larger surplus.



Hunting gathering



Slave ownership



Feudalism



Capitalism

Something else?

# The Economic Surplus

- Every economy must produce enough to keep its participants alive, and to allow production to continue next year.
  - Subsistence for the people.
  - Replace inputs to production (eg. seeds for next year's crop).
- Production above and beyond this is the “economic surplus.”
  - It can be consumed, invested, or wasted.
  - Control & use of the surplus is a key dimension of economic organization.
  - Different economic systems do it differently.

# Common Themes & Lessons

- Work is the source of all value added, no matter what the economic system.
- Humans learn by doing: as we work, we learn how to work better (technology).
- Social relationships and the organization of our work change with technology.
- Every society which produces a surplus, must decide who gets it, and what they do with it.
- Nothing in the economy is permanent.
  - Attempts to portray capitalism as “natural” or “ever-lasting” are ideological.

# Capitalism: Just One Kind of Economy

- All economies require work to be done to produce the goods & services we need.
- But they organize that work (and the distribution & use of output) differently.
- Our economy today does that in a particular, peculiar way.
- It's called "capitalism."
- Strange irony: mainstream economics almost never mentions the word "capitalism."
  - They assume that it's a "natural state of affairs."
  - But that's wrong: capitalism is a historical stage.

# Capitalism: ...the “C” Word



# The Two Defining Features of Capitalism

1. Most production is initiated & undertaken by private companies who aim to generate profit from this activity.
  - “Production for profit.”
2. Most work is performed by individuals who work for someone else in return for money (wages or salaries).
  - “Wage labour.”
  - We call this type of work “employment.”

# Capitalism and its Euphemisms

- Usually called a “market economy” in textbooks (when it is given a name at all).
- This reflects the narrow focus of conventional (neoclassical) economics.
  - Tries to explain all behaviour as optimizing market transactions.
- But other economies have markets.
- And many things in capitalism are not determined through markets.
  - Especially inside a firm.

# The Birth of Capitalism

- The economic system we live under now emerged in the 18<sup>th</sup> Century in western Europe (especially Britain).
- It emerged from more advanced and centralized feudal monarchies.
  - Non-agricultural production and trade came to displace feudal agriculture as most influential sector in society.
  - New forms of ownership and control arose to reflect new technology of work.
  - New social structures emerged to meet the needs of this new system.

# What “Caused” Capitalism

Several factors contributed to the emergence of capitalism...

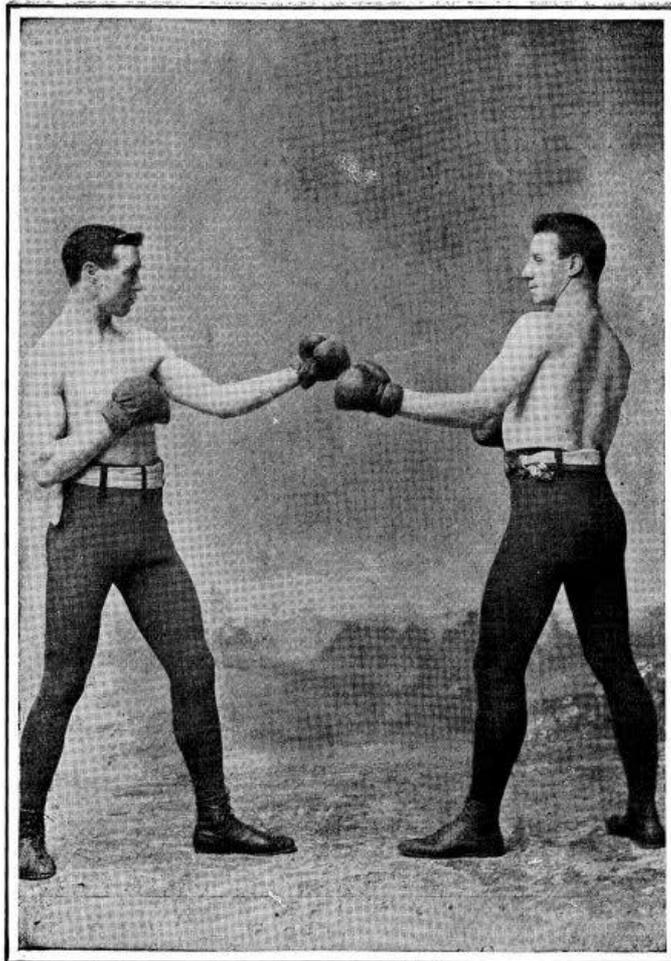
... and its initial concentration in W. Europe.

- Technology (power systems, machinery).
- Unified, reliable markets (transport networks, weights & measures).
- Resources (water power, coal).
- Empire (raw materials & slave labour from colonies; captive market for output).
- Government (strong state to oversee commerce, protect private property, manage colonies).

# The Evolution of Capitalism

- Initial conditions in capitalism were very harsh.
- Capitalism rapidly spread and evolved.
  - Very high profits & high rates of reinvestment, kept the system growing and dynamic.
- Conditions improved (in many places, not all), reflecting:
  - Social conflict
  - Wars
  - Booms and busts
  - Democratization
- Capitalism has experienced distinct phases.
- In the last century these phases included:
  - Early boom
  - Great Depression
  - Postwar “Golden Age”
  - Neoliberalism

# Neoliberalism: Capitalism with the Gloves Off





# Key Goals of Neoliberalism

(p.49)

- Reduce and control inflation; protect the value of financial wealth.
- Restore insecurity and “discipline” to labour markets.
- Eliminate “entitlements”; force families to fend for themselves.
- Roll back and refocus government activities to meet business needs; cut taxes.
- Generally restore the economic and social dominance of private business and wealth.
- Claw back expectations; foster a sense of resignation to insecurity and hardship.

# Key Tools of Neoliberalism

(p.49)

- Use interest rates aggressively to regulate inflation and control labour markets.
- Privatize and deregulate more industries.
- Scale back social security programs (especially for working-age adults).
- Deregulate labour markets (including attacks on unions).
- Use free-trade agreements to expand markets and constrain government interventions.

# Kinds of Capitalism

- Even under neoliberalism and globalization, different “varieties” of capitalism have been maintained.
  - With very different social and environmental effects.
- 1. Anglo-Saxon model (most unequal)
- 2. Continental model
- 3. Asian model
- 4. Scandinavian model (most equal, inclusive)
- Fighting for improvements in capitalism is possible and important
  - But is it enough??

***See chart p. 50.***

<i>Type of Capitalism</i>	<i>Role of Government: Taxes as Share GDP</i>	<i>Role of Government: Economic Regulation</i>	<i>Financial Sector (Banks, Stock Market)</i>	<i>Income Distribution</i>	<i>Managing Income Distribution</i>	<i>Union Coverage as % Workforce</i>
<b>Anglo-Saxon</b> (US, UK, Canada, Australia)	30-35%	Weak	Very Large	Very Unequal	Market Power	10-30%
<b>Continental</b> (France, Germany, Italy)	35-45%	Moderate	Moderate	Somewhat Equal	Mild Corporatist <sup>¶</sup>	50-90%
<b>Asian</b> (Japan, Korea, China)	25-35%	Strong <sup>†</sup>	Relatively Small	Somewhat Equal	Paternalist Corporatist <sup>¶</sup>	10-20%
<b>Nordic</b> (Sweden, Norway, Denmark, others*)	45-55%	Strong	Relatively Small	Very Equal	Strong Corporatist <sup>¶</sup>	50-80%

\* Some other European countries (like Austria and the Netherlands) have features similar to the Nordic type.

† The state is especially active in the Asian model in stimulating capital investment and managing the sectoral make-up of the economy.

¶ CORPORATISM refers to a system of centralized negotiation between business, labour, and government.

# How Capitalism Works

- Like it or hate it, most of the world economy today is capitalist.
  - And whether you like it or hate it, you need to understand how it works.
  - That will help us get the most out of it, and change it (as needed).
- The key features of capitalism (production for profit and wage labour) tend to produce & reproduce key behaviours over time, including:
  - Competition
  - Growth
  - Innovation
  - Conflict
  - Inequality
  - Cycles

# Demystifying “Capital”

- “Capital” is just the economic term for “tools.”
- Physical capital: real, tangible products used to produce other products.
  - Distinct from “financial capital,” which is just money.
- Fixed capital: long-lived, used in a workplace.
  - **Structures**: buildings, offices, stores.
  - **Machinery and equipment**: computers, assembly lines, hand tools, transportation equipment.
  - **Infrastructure**: roads, bridges, utilities.
- Working capital: the value of raw materials, inventories, and other items used up in production.

# The Private Company

- One of the defining features of capitalism: most production is undertaken for private profit
- The private company is the entity through which that profit-seeking activity is organized
- Private companies come in all shapes and sizes:
  - Large global corporations
  - Medium-sized firms (most work done by paid workers)
  - Very small firms (most work done by owner & family)
- All companies have two key features:
  1. Somebody owns them, and hence claims its profits
  2. The owner directs the firm in their interests

# Types of Companies

- Individual proprietorships
  - Individual owner owns & controls it directly
- Partnerships
  - Joint owners share the investment & profit
- Corporations
  - Separate legal entity which limits the liability and potential losses of the owners
  - Large corporations are usually owned through joint-stock (issuing equity shares)
  - The biggest global corporations are economically larger than many countries, and operate through tight central plans

# The Biggest of the Big

(p.90)

<b>Category</b>	<b>Large Company</b>	<b>Equivalent Country</b>
<b>Value-Added</b>	<i>ExxonMobil</i> <i>(\$195 billion)</i>	<i>Finland</i> <i>(\$195 billion)</i>
<b>Employment</b>	<i>Wal-Mart</i> <i>(2.3 million)</i>	<i>New Zealand</i> <i>(2.3 million)</i>
<b>Cash</b>	<i>Apple Inc.</i> <i>(\$147 billion)</i> <i>(Cash &amp; securities)</i>	<i>U.S. Fed Govt</i> <i>(\$110 billion)</i> <i>(official reserves)</i>
<i>2013 data, \$US.</i>		

# Who Owns Corporations?

- Ownership of joint stock companies is dispersed
  - Shares are bought & sold on the stock market
- Problem: how to ensure company acts in owners' interests
  - Problem solved through major share ownership and executive compensation
  - Top managers of the firms are major owners, with huge personal stake in share price
- Ownership of business wealth as a whole is concentrated among a small elite
  - It's a myth that the stock market, mutual funds, etc., have allowed everyone to become "owners"

# The Shocking Concentration of Business Wealth

Distribution of Financial Wealth				
	Top 10%	Top 1%	Billionaires	Bottom 50%
Canada	58%	n.a.	5% (54)	3%
U.S.	71%	34%	6% ( $\approx$ 500)	2%
Australia	53%	n.a.	7% (37)	6%
U.K.	71%	34%	10% (169)	1%
World	57%	32%	n.a.	4%

- *Most financial wealth is owned by the top 10%.*
- *The bottom 50% own almost no financial wealth.*
- *A handful of billionaires own more than the majority.*

# The Logic of Profit

- Competition forces companies to meet the “going rate” of profit or go out of business
  - This imposes a logic & discipline on the system
  - This logic (not the personal views and actions of CEOs) explains why capitalism does so much harm
- Under capitalism (“production for profit”) something is done if it is profitable
  - Not necessarily if it is useful
- We cannot assume that profitability is a measure of an activity’s value
  - “Production for profit” does not guarantee that human needs are being met

# The Logic of Profit

- Think of something that is profitable but not useful.
- Mention it in the chat.
- One example:





Right then, it looks like we've agreed on our corporate mission statement: *"to make money, wads of it, and pay as little income tax as possible."*

# Purposes of a map:

- Where are you?
- Where do you want to go?
- How will you get there?



# Drawing the Map: The Core Elements

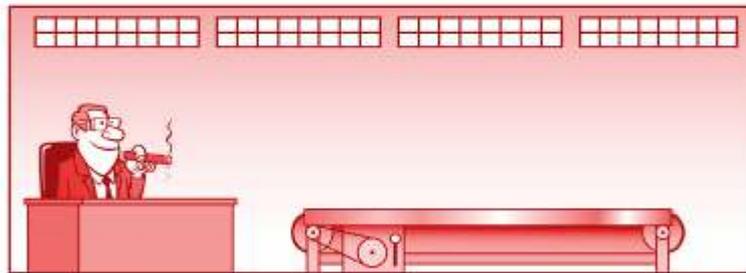
- We have introduced several key economic concepts:
  - Workers and capitalists
  - Investment
  - Work and production
  - Consumption and reproduction
  - Profit
- Let's assemble them into a picture of the core “circle” of capitalism.



**It all starts with our  
“capitalist” (or, more  
precisely, the “major owners  
and top managers”).**

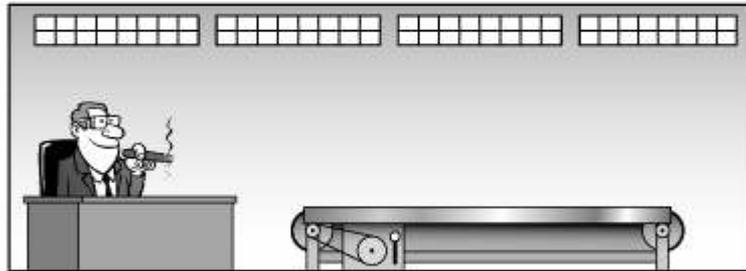


Seeking profit,  
he or she  
decides to  
make an initial  
investment (I).



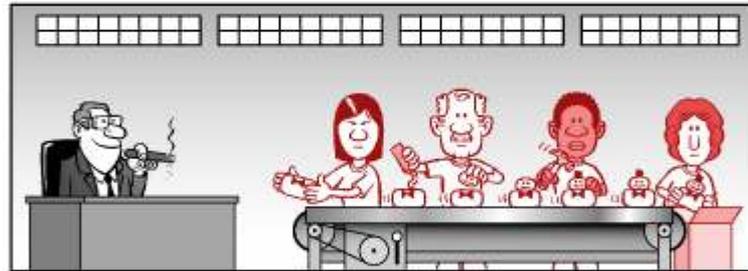
**The investment is used to purchase real capital goods and set up a workplace.**

**But notice that nothing is happening yet in this workplace.  
(...Why not?)**



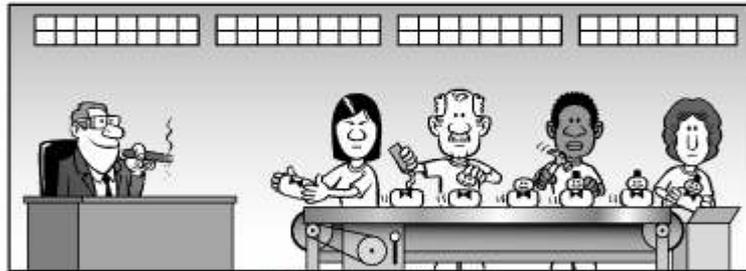
**Work requires  
workers. They  
live in the  
working class  
neighbourhood.**

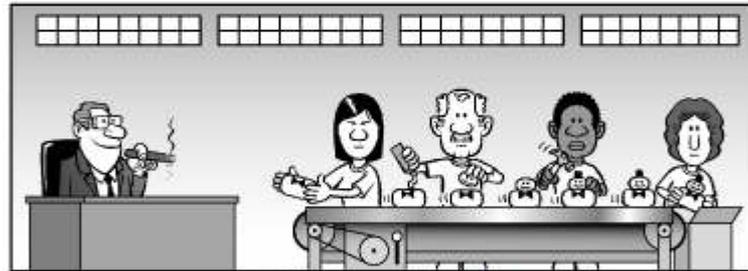




The workers are hired, and only then can production begin. NOW something is finally happening!

**WHY** do the workers agree to work? Not for the joy of it. Rather, they seek to earn wages ( $W$ ) through wage labour in order to live. They have no other way to support themselves.

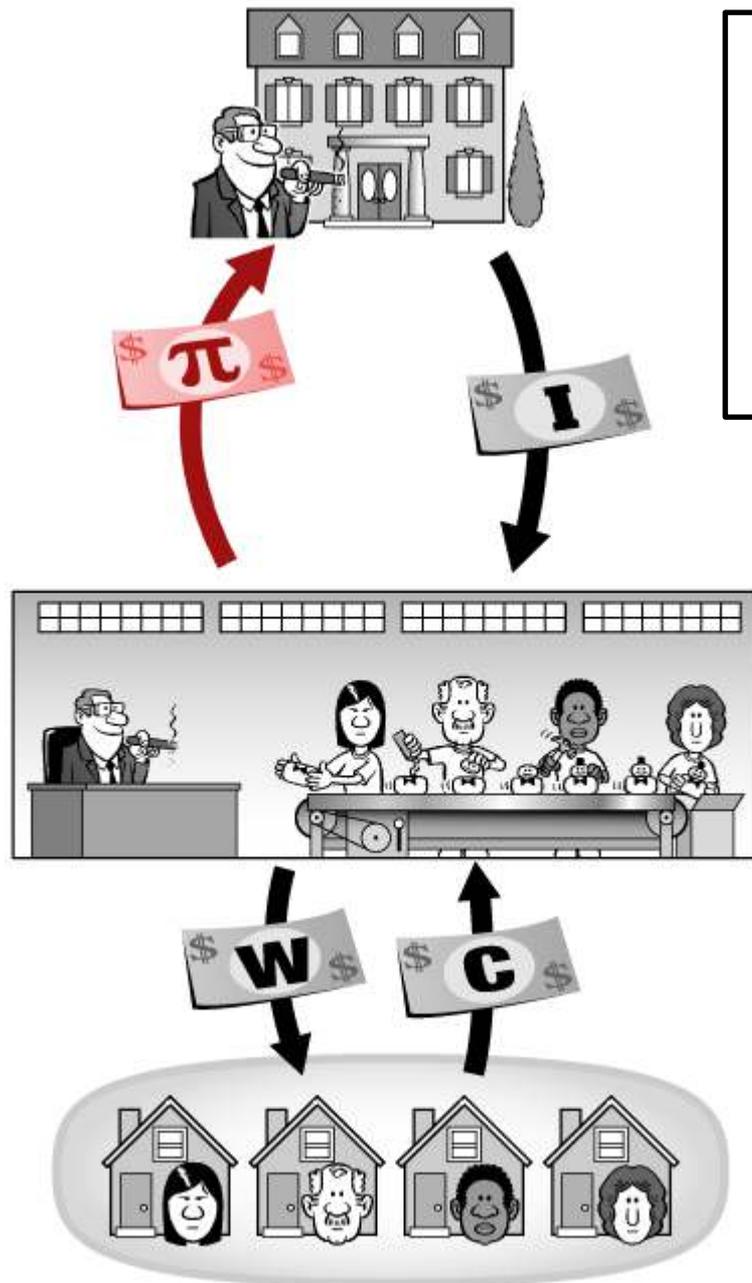




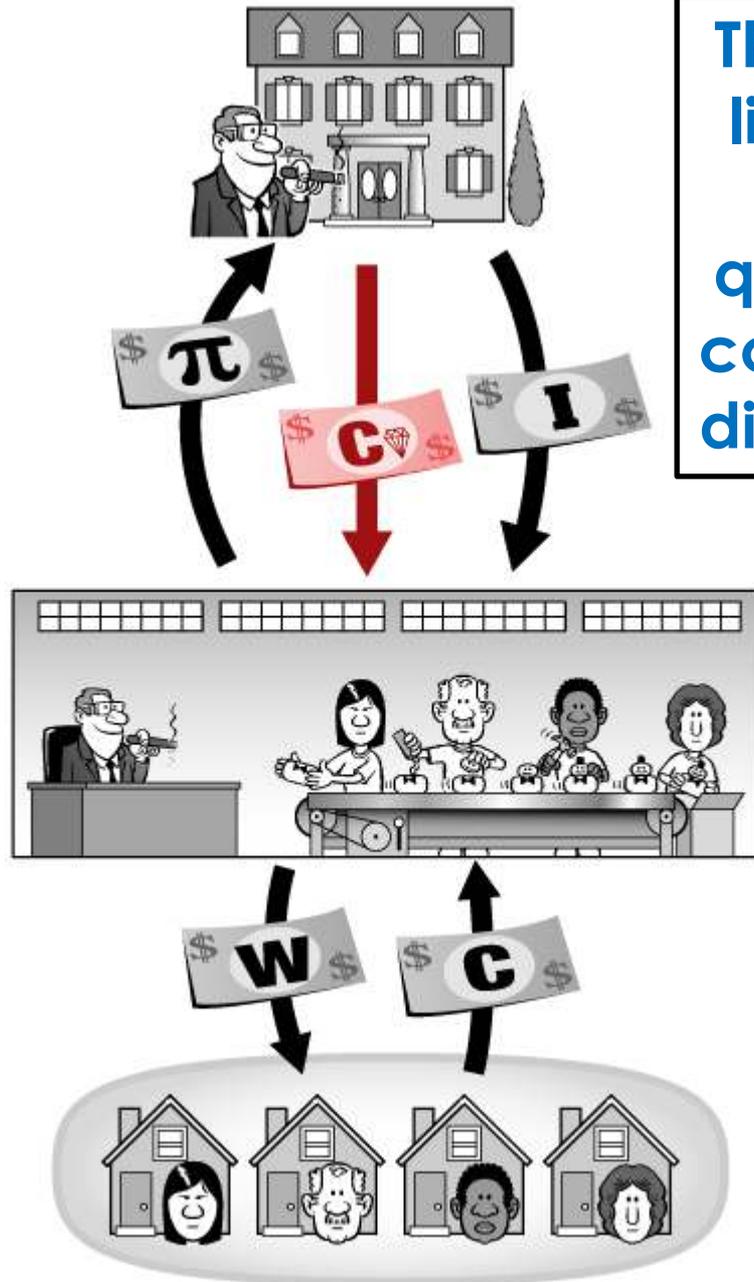
Workers spend essentially all their income on consumption (reproduction). This is summarized in the slogan: “Workers spend what they get.”

With their wages they purchase the consumer goods and services (C) that (together with unpaid labour in the home) allows for their reproduction.

After the bills are paid (especially wages for the workers), the capitalist gets what's left over as profit (symbolized by the Greek letter pi,  $\pi$ ).

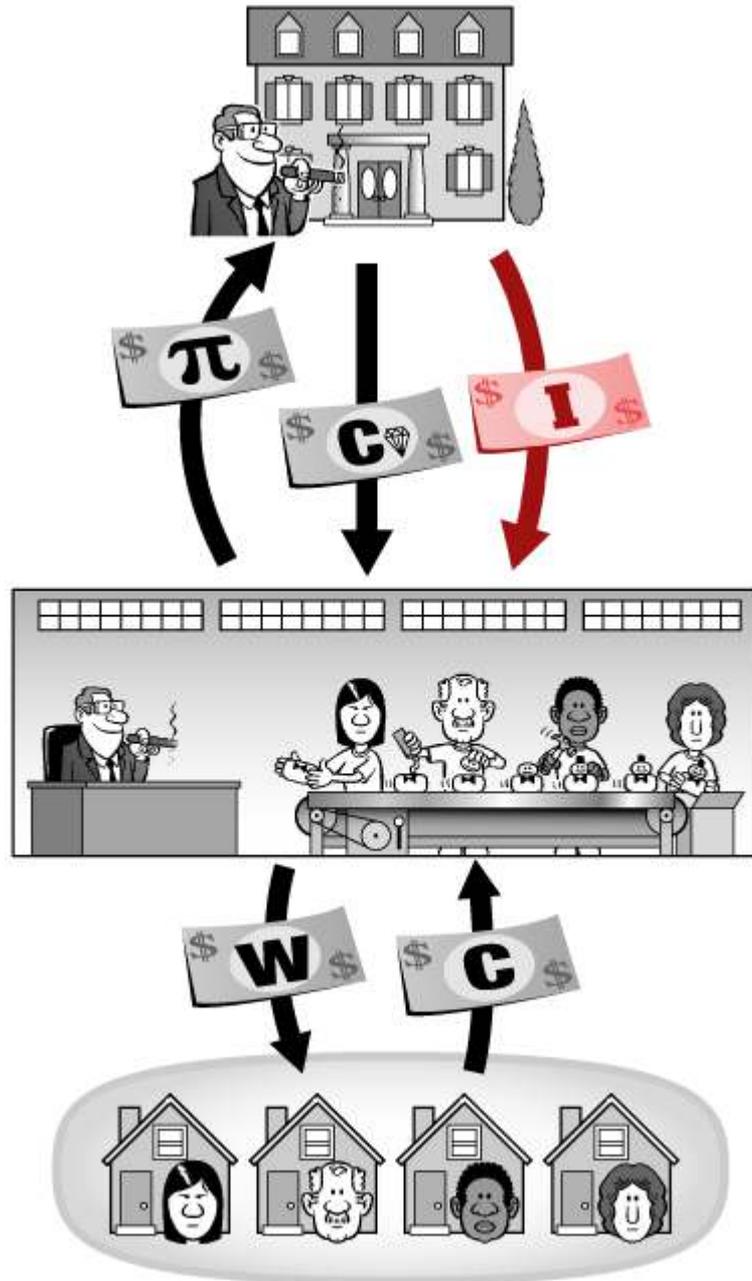


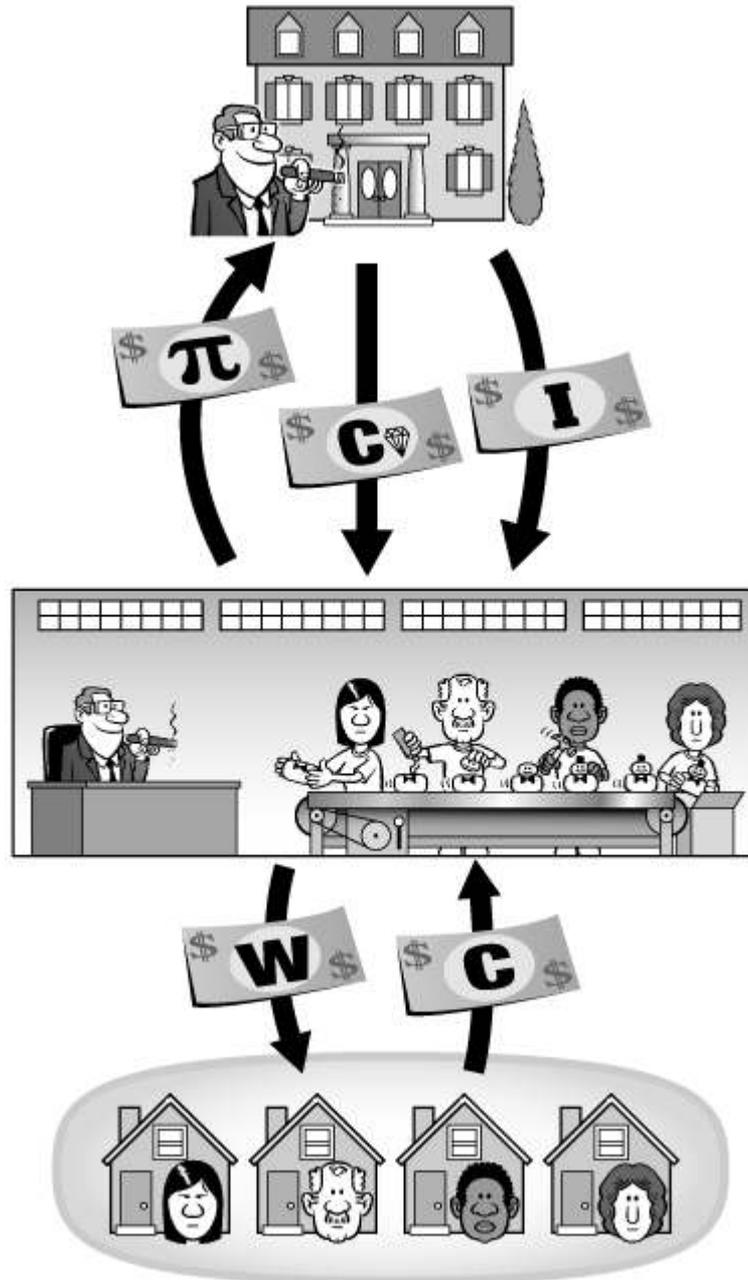
After all, that profit was the point of investing in the first place!



The capitalist also likes to consume (usually high-quality stuff). Their consumption ( $C$ ) is diamond-studded!

Finally, if the whole process has unfolded suitably, and the capitalist received a healthy profit, then he starts the whole cycle over again with another investment.





**Ta-da!**  
That's the  
"little circle" of  
capitalism. It  
portrays the  
core  
relationships  
at the centre  
of the whole  
system.

# What We Learned From This Simple Map

- There are two dominant classes in society.
- The capitalist's investment is the initial force that starts the cycle going.
- Workers work to survive – and their wages are how they pay for survival.
  - And hence their income, once generated, is immediately pumped back into the economy in the form of consumption spending.
- The economy is a circular process:
  - Investment  $\Rightarrow$  production  $\Rightarrow$  income  $\Rightarrow$  consumption  $\Rightarrow$  profit
  - This cycle repeats itself over and over again

# Income and Spending

- For the whole cycle to be completed (and then started again), the capitalist must sell all their output.
- In other words, all income generated in production, must be spent, in order for:
  - All output to be purchased.
  - The capitalist to receive (or “realize”) their profit.
- This balance between income and expenditure is very important to the smooth functioning of the cycle.

# Income and Expenditure: The Little Circle *(p.132)*

<b>Class</b>	<b>Income</b>	<b>Expenditure</b>
Workers	Wages (W)	Consumption (C)
Capitalists	Profits ( $\Pi$ )	Investment and Luxury Consumption ( $I + C_{\diamond}$ )
<b>Total Economy</b>	<b><math>W + \Pi</math></b>	<b><math>C + C_{\diamond} + I</math></b>

The capitalist has 3 potential markets to sell their output: mass consumption, luxury consumption, and investment goods (capital equipment). They must sell all their output into one of those markets.

# Making it Work

- This is a simple map.
- But it captures the essence of capitalism:
  - Production is motivated by profit-seeking investment.
  - Work is performed by wage labourers.
- And now we see what's required for capitalism to successfully function:
  - Initial investment by the capitalist.
  - Successful work by the workers.
  - The successful sale of all output.
- If capitalist is optimistic, it happens again

**Thank You!**

***Let's take 5 minutes...***