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From the Classical School to Today: The Evolution of Stagnation Theories

Francis J. Lukacovic II

State University of New York College at Buffalo - Buffalo State College, franklukacovic@gmail.com

Advisor

William T. Ganley, Ph.D., Professor of Economics

First Reader

William T. Ganley, Ph.D., Professor of Economics

Second Reader

Ted P. Schmidt, Ph.D., Associate Professor of Economics

Third Reader

Bruce L. Fisher, J.D., Visiting Professor and Director

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From The Classical School to Today: The Evolution of Stagnation Theories

by

Francis J. Lukacovic II

An Abstract of a Thesis
in
Applied Economics and Finance

Submitted in Partial Fulfillment
of the Requirements
for the Degree of

Master of Arts

May 2016

Buffalo State College
State University of New York
Department of Economics and Finance

ABSTRACT OF THESIS

The purpose of this thesis is to study the theory of secular stagnation, which was made famous by the American Keynesian economist Alvin Hansen in his book Full Recovery or Stagnation. The theory of secular stagnation has reappeared in economic circles today due to recent economic conditions since the financial crisis of 2007-2008. The thesis will analyze the history of the stagnation theory dating back to Classical economists in the 19th century. The concept of a stagnating economy has been talked about for centuries with many economists adding important thoughts. Furthermore, the thesis will address the current questions and examine whether the stagnation claims have merit in today's economy. High unemployment and slow economic growth in developed countries including the United States may be explained by the theories of secular stagnation and the matured economy.

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Approved by:

William T. Ganley, Ph.D.
Professor of Economics and Finance/Thesis Adviser

Frederick Floss, Ph.D.
Chair and Professor of Economics and Finance

Kevin Railey, Ph.D.
Associate Provost and Dean of the Graduate School

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Chapter One: Introduction

Recently, there has been a renewed discussion on the idea of secular stagnation. The recovery from the great recession of 2008 has seen the economy experience low growth and a slow decline in unemployment. Secular stagnation, a term introduced to us by Alvin Hansen, an American economist is the idea that the economy has stagnated due to structural changes and is not just a normal downturn in a business cycle.

In 2013, former Treasury Secretary and former National Economic Council director Lawrence Summers made a case that the United States could be facing secular stagnation at an International Monetary Fund conference. Since then, there has been plenty of discussion on the theory. Summers has gone back and forth with former Chairman of the Federal Reserve, Ben Bernanke on the validity of the theory in today's world.

The idea of a stagnating economy is not new. It dates back to Classical economists of the eighteenth and nineteenth century. A theory of population introduced by Thomas Malthus served as a basis for stagnation theories from various economists of the Classical era. Karl Marx also developed a theory of stagnation as well, expanding on the ideas from Classical economists. Next, Thorstein Veblen developed his own stagnation theory. Lastly, we get to Keynes and Alvin Hansen who developed the most advanced theory of stagnation.

In this thesis, we will examine the evolution of the various stagnation theories and look to the writings of these prominent economists to explain each school of thought's theory. Also, we will examine any solutions that each economist proposed as a way to avoid stagnation in a capitalist economy.

Chapter two will be devoted to the study of the Classical school and their views on capitalistic stagnation. First, we will explain the Malthusian theory of population to provide a basis for the Classical school of thought. Then, we can continue to examine the theories of John Stuart Mill and David Ricardo. In Chapter three, we examine Marx's outlook on the future of capitalistic society and his theory of stagnation. Chapter four will introduce Institutional economics and the writings and ideas of Thorstein Veblen. We will analyze his thoughts on stagnation. Chapter five deals with John Maynard Keynes and how his analysis of the economy has an underlying idea of stagnation. In Chapter six, we get to the idea of secular stagnation and the matured economy. Alvin Hansen contributed a lot to these ideas which are still important today. Chapter seven dissects the debate today between Lawrence Summers, Ben Bernanke, and others. And finally in Chapter eight, we have concluding remarks.

Chapter Two: Classical Economists on Stagnation

The early theories of stagnation put forward by Classical economists were, by a large extent, based on Thomas Malthus' argument in An Essay on the Principles of Population. So, we will first analyze these principles before presenting the stagnation theories of David Ricardo and John Stuart Mill.

The Malthusian theory of population states that the means of subsistence limits the population of the earth and that the food supply will increase in an arithmetical ratio, while the population will increase in a geometrical manner (Malthus I, 1933, pp. 8-10). Therefore, the food supply would not be able to keep up with population growth over the long term. Malthus revised his theory of population in the second edition, but some economists failed to address this in their economic writings. In later editions of the Principles of Population, he denied that the 'Law of Diminishing Returns' would lead civilization to a gloomy end. Instead, he proposed that man may take precautions to prevent this end of society (Malthus I, 1933, pp. 341).

Malthus would go on to explain, in the first edition, his opinion on the growth of population and the food supply with:

The necessary effects of these two different ratios of increase, when brought together, will be very striking. Let us call the population of this island 11,000,000; and suppose the present produce equal to the support of such a number. In the first twenty-five years the population would be 22,000,000, and the food being doubled, the means of subsistence would be equal to the increase. In the next twenty-five years, the population would be 44,000,000, and the means of subsistence only equal to the support of 33,000,000. In the next period the population would be 88,000,000, and the means of subsistence just equal to the support of one-half that number. And, at the conclusion of the first century, the population would be 176,000,000 and the means of subsistence only equal to the support of 55,000,000, leaving the population of 12,000,000 totally unprovided for (Malthus II, 1933, pp. 126-127).

Up until the publication of Malthus' An Essay on the Principles of Population, political economy had upheld the optimistic outlook that Adam Smith had introduced in The Wealth of Nations. Adam Smith insisted "every increase in the stock or revenue of society as increase in the funds for the maintenance of labor" (Malthus, 1933, pp. 128-129), but Malthus rejected this idea and held "that the funds for the maintenance of labor do not necessarily increase with the increase of wealth, and very rarely increase in proportion to it" (Malthus, 1933, p. 129).

The Malthusian theory of population began to catch on with political economists and industrialists. E.A.J Johnson described this fascination clearly in his book Some Origins of the Modern Economic World:

The Malthusian theory of population fell like Mana from Heaven into the hands of English capitalists. Here was a convenient explanation of poverty and low-wages, a body of social theory supported by an imposing parade of facts which proved the universality of a 'Natural' principle of population. Here then was a philosophical fount in which factory owners could wash their unclean hands. Low wages had their origin in the 'passion between the sexes' which resulted in a natural tendency for population to outstrip the food supply. For these conditions surely the employer of labor could not be held responsible; in fact, he was rather a social benefactor who have employment to a large number of those super-poor. The real culprits were the parents who, by failing to curb their reproductive propensities, had brought into existence these unfortunate children whom factories employed (Johnson, 1938, pp. 108-109).

The Malthusian theory of population laid the foundation for the Classical School's stagnation theory. Classical Economists such as David Ricardo and Alfred Marshall have held that production is limited by 'The Law of Supply and Demand' and 'The Law of Diminishing Returns.' The Malthusian theory of population reveals the 'The Law of Diminishing Returns', as it states that as additional amounts of capital or labor are added to production past an optimum point the profits to be gained will be less and less with each addition of capital or labor (McConnell, 1947, p. 121).

Now that we have explained some of the ideas presented in Malthus' An Essay on the Principles of Population, we can now understand the Classical School's theory of stagnation better. More specifically, we will examine the views of David Ricardo and John Stuart Mill.

David Ricardo's Stagnation Theory

Classical economist David Ricardo develops his theory of stagnation in his Principles of Political Economy and Taxation. He develops the stagnation theory that was underlying in the works of Malthus and his predecessors. Through Ricardo's theory of rent and his examination of the tendency of profits to fall in manufacturing, his stagnation theory is given life.

In his theory of differential fertility of land, Ricardo accepts Malthus' establishment of 'The Law of Diminishing Returns'. This creation of the differential fertility of land leads to one of Ricardo's arguments that the economy of a capitalistic society will end in stagnation. John W. McConnell describes Ricardo's idea of rent:

Rent is that portion of the produce of the earth which is paid to the landlord for the use of the earth which is paid to the landlord for the use of the original and indestructible powers of the soil. There is no rent when land of nearly equal fertility is present in sufficient abundance to supply human demands. When an increase in population causes land of inferior quality and less advantageous situation to be called into cultivation, then rent is paid. Assuming the presence of land of three degrees of quality, let us suppose an increase in population creates a demand for food, making it necessary to call into cultivation the land of the second quality. The greater the costs of production, either in labor or transportation, will cause the price to rise. Obviously, the smaller costs of production on the first quality land in relation to the price paid for each unit of the product will yield a surplus to the first land over the second. This, says Ricardo, is rent. If further increase in population brings the land of the third quality into production, rent on both first and second quality land will rise. The price of natural products will be determined by the higher labor costs necessary to produce the additional quantities needed under the least favorable circumstances (McConnell, 1947, pp. 55-56).

Ricardo showed that differential rents on land of several qualities tended to drive down profits. If the falling rate of profit of a farmer merely hurt him, it would not force the economy

into stagnation; however, “there are few commodities which are not more or less affected in their price by the rise of raw produce, because some raw material from the land enters into the composition of most commodities” (Ricardo, 2001, p. 90).

Ricardo said the natural rates of profits is to fall based on his examination of “The Law of Diminishing Returns’ and his theory of the differential fertility of land. He summarized:

The natural tendency of profits, then is to fall; for, in the progress of society and wealth, the additional quantity of food required is obtained by the sacrifice of more and more labor. This tendency, this gravitation as it were of profits, is happily checked at repeated intervals by the improvements in machinery connected with the production of necessities, as well as by the discoveries in the sciences, which enables us to relinquish a portion of labor before required, and therefore to lower the price of the prime necessities of the laborer. The rise of labor is, however, limited; for as soon as wages should be equal to 720 pounds, the whole receipts of the farmer, there must be an end to accumulation, for no capital can yield any profit whatever, and no additional labor can be demanded and consequently population will have reached its highest point (Ricardo, 2001, pp. 96-99).

Ricardo contended that without improved technology the economy would end in stagnation because of the difference in profits to be derived from lands of differing qualities. He also later argues in Principles of Political Economy and Taxation that increased technology will only prevent stagnation for a brief period of time. Ricardo was of the opinion that the discrepancy between fixed and circulating capital would drive the economy into stagnation, this despite improvements were made in the state of industrial arts:

Were it true that the proportion between these two sorts of capital is the same at all times, and in all countries, then indeed, it follows that the number of laborers employed is in proportion to the wealth of the state. But such a proposition has not the semblance of probability. As arts are cultivated, and civilization is extended, fixed capital bears a larger and larger proportion to circulating capital. The amount of fixed capital employed in the production of a piece of British muslin is at least a hundred times, probably a thousand times greater than that employed in the production of a similar piece of Indian muslin. And the proportion of circulating capital is a thousand times less. It is easy to conceive that under certain circumstances, the whole of the annual savings of an industrious people might be added to fixed capital, in which case they would have no effect in increasing the demand for labor (Ricardo, 2001, pp. 385-387).

With his acceptance of the Malthusian law of population and the differential theory of rent, and his theory of the downward trend of profits due to the discrepancy between fixed and circulating capital, Ricardo described a very bleak future of the capitalistic society. Eric Roll summarizes Ricardo's views compared with other Classical economists in his History of Economic Thought:

It has been the fashion in recent years to regard Ricardo's work as the most distinct exposition of the beliefs contained in the classical theory that the economic system automatically achieved full employment and market equilibrium through time, and that fluctuations of economic activity or prolonged stagnation were impossible. Closer examination reveals, however, that Ricardo's analysis, because it penetrated to greater depths than did that of his contemporaries, was by far the least polished statement of these classical beliefs. It left open many problems to which subsequent theories of crises and under-employment could be attached. Many theories of technological unemployment or of disproportions in the structure of production can be traced back to the views enunciated by Ricardo. And the Marxian theory of crises, too, has a close connection with Ricardo's theory of economic development (Roll, 1942, pp. 204-205).

We will later look at the Marxian theory of stagnation but now we will examine the stagnation theory of John Stuart Mill.

John Stuart Mill's Stagnation Theory

Next, we will examine the works of John Stuart Mill in an attempt to discover his thoughts on the prospect of a stagnating economy. Mill's theory of stagnation also grows out of the Malthusian theory of population growth and he also thought the loss of savings would drive the economy into stagnation as Classical economists believed all funds for investment must be derived from the savings of the community. The modern-day concept of banks creating money through loans was not a practiced (McConnell, 1947, pp. 150-160).

The capacity of increase is necessarily in a geometrical ratio; the numerical ratio is different.

To this property of organized beings, the human species forms no exception. Its power of increase is indefinite, and the actual multiplication would be extraordinarily rapid, if the power were exercised to the utmost. It is never exercised to the utmost and yet, in the most favorable circumstances known to exist, which are those of a fertile region colonized from an industrious and civilized community, population has continued, for several generations, independently of fresh immigration, to double itself in not much more than twenty-five years (Mill, 1965, pp. 153-155).

Besides the Malthusian law of population growth, Mill also believed that the 'Law of Diminishing Returns' would also ultimately lead to a stationary state. He wrote in his Principles of Political Economy:

Though the general thriftiness of the laboring class is much below what is desirable, the spirit of accumulation in the most prosperous part of the community requires abatement rather than an increase. In these countries there would never be any difficulty of capital, if its increase were never checked or brought to a stand by too great diminution of its returns. It is the tendency of the returns to a progressive diminution, which causes the increase of production to be often attended with a deterioration in the conditions of the producers; and this tendency, which would in time put an end to increase of production altogether; is a result of the necessary and inherent condition of the production from the land (Mill, 1965, pp. 187-88).

Despite there being a plethora of capital and technical knowledge at the time, Mill still held a pessimistic outlook of the future due to his belief in the ‘Law of Diminishing Returns’.

When a country has long possessed a large production, and a large net income to make savings from and when, therefore, the means have long existed of making a great annual addition to capital; it is one of the characteristics of such a country that the rate of profit is habitually within as it were, a hand’s breadth of the minimum, and the country therefore on the very verge of the stationary state (Mill, 1965, p. 446).

According to Mill, the only way to cure stagnation would be to cut the wages of the laborer or to force into the labor market those persons not engaged in productive labor. However, Mill’s suggestions were not seriously believed by himself or his followers.

On the whole, therefore, we may assume that in such a country as England, if the present amount in such a country as England, if the present amount of savings were to continue, without any of the counteracting circumstances which now keep in check the natural influence of those savings in reducing the profits, the rate of profit would speedily attain the minimum, and all further accumulation of capital would for the present case (Mill, 1965, p. 448).

When Adam Smith published The Wealth of Nations in 1776, he created an optimistic spirit of capitalism. But within less than one hundred years, we find John Stuart Mill, a follower of Smith having a much more pessimistic view due to his view of the tendency of profits to fall and the ‘Law of Diminishing Returns’. Mill summarized his negative view:

This impossibility of ultimately avoiding the stationary state – this irresistible necessity that the stream of human industry should finally spread itself out into an apparently stagnant sea – must have been, to the political economists of the last two generations, an unpleasing and discouraging prospect, for the tone and tendency of their speculation goes completely to identify all that is economically desirable with the progressive state (Mill, 1965, pp. 451-452).

David Ricardo saw capitalistic society headed towards stagnation because of the differential rates of rent on lands of differing qualities and because of the discrepancy between fixed and circulating capital.

John Stuart Mill believed capitalistic society stagnating due to the 'Law of Diminishing Returns', the Malthusian theory of population, and the loss of investment funds for the improvement of the country.

Chapter Three: Marxian Economics on Stagnation

In the previous chapter, we showed that David Ricardo in his Principles of Political Economy and Taxation and John Stuart Mill in his Principles of Political Economy believed that capitalistic society would end in stagnation. They based their theories on the Malthusian principles of population, ‘The Law of Diminishing Returns’, and the tendency for profits to fall because of the discrepancy between fixed and circulating capital.

Karl Marx and his followers saw the future of capitalism in a very negative light. They believed it would eventually lead to an economy of stagnation, privation, and general misery amongst people. We will now look into the reasoning and theory behind Marx’s belief in stagnation.

Marx, in the first volume of Capital, rejected the validity of the Malthusian theory of population. Marx stated that “an abstract law of population exists for plants and animals only, and only insofar as man has not interfered with them” (Marx, 1909, p. 271). He did speak on a “surplus population” however:

The production of a relative surplus-population, or the setting free of laborers, goes on therefore yet more rapidly than the technical revolution of the process of production that accompanies, and is accelerated by, the advances of accumulation; and more rapidly than the corresponding diminution of the variable part of capital as compared with the constant. If the means of production, as they increase in extent and effective power, become to a less extent means of employment of laborers, this state of things is again modified by the fact that in proportion as the productiveness of labor increases, capital increases its supply of labor more quickly than its demand for laborers. The overwork of the employed part of the working class swells the ranks of the reserve, whilst conversely the greater pressure that the latter by its competition exerts on the former, forces these to submit to overwork and to subjugation under the dictates of capital. The condemnation of one part of the working-class to enforced idleness by the overwork of the other part, and the converse becomes a means of enriching the individual capitalists, and accelerates at the same time the production of the industrial reserve army on a scale corresponding with the advance of social accumulation (Marx, 1947, 697-699).

He believed that capitalistic society would be forced into stagnation by ‘The Industrial Reserve Army of the Unemployed’, and by the ‘Law of the Increasing Misery of the Proletariat’. Marx, in analyzing a formula of growth saw capital as an independent variable and labor as a dependent variable. Over time, capital will control labor because of technological advancements. The disposable industrial army reserve would continue to grow as technology improves leading to a lower return on surplus-value.

But if a surplus laboring population is a necessary product of accumulation or the development of wealth on a capitalist basis, this surplus production become, conversely, the lever of capitalistic accumulation, nay, a condition of existence of the capitalist mode of production. It forms a disposable industrial reserve army, that belongs to capital quite as absolutely as if the latter had bred it at its own cost. Independently, of the limits of the actual increase of population, it creates, for the changing needs of the self-expansion of capital, a mass of human material always ready for exploitation. With accumulation, and the development of the productiveness of labor that accompanies it, the power of sudden expansion of capital grows also. The mass of social wealth, overflowing with the advance of accumulation, and transformable into additional capital, thrusts itself frantically into old branches of production, whose market suddenly expands, or into newly formed branches, such as railways, the need for which grows out of development of the old ones. In all such cases, there must be the possibility of throwing great masses of men suddenly on the decisive points without withdrawing them from the other branches of production. Overpopulation supplies these masses. The course characteristic of modern industry, *viz.*, a decennial cycle (interrupted by smaller oscillations) of periods of average activity, production at high pressure, crisis and stagnation, depends on the constant formation, the greater or lesser absorption, and the reformation of the industrial reserve or surplus population (Marx, 1909, pp. 275-277).

In his theory of surplus-value, Marx found his way to a conclusion of capitalistic exploitation of the working class, which is also found in the works of John Stuart Mill and David Ricardo. John McConnell described Marx’s theory of surplus value as:

Labor is paid on the basis of its physical reproduction and maintenance costs; but the laborer is required to work hours over and above the necessary to meet these costs. Thus every additional hour that he works above the point necessary to produce sufficient articles to supply the laborer’s reproduction and maintenance costs (his wages), he is producing

value which is appropriated by the employer. This value above his reproduction and maintenance costs is surplus-value (McConnell, 1947, pp. 33-34).

The Marxian theory of stagnation also focuses on the theory of constant and variable capital. Constant capital referred to the value of the part of capital put out by the capitalist for acquiring means of production, such as, raw and auxiliary materials, and instruments of labor is therefore not altered in the course of the process of production. Variable capital is the value of the part of capital used to purchase labor power and is altered during the process of production. It reproduces its own value and yields a surplus-value over and above constant capital. This surplus-value can be greater or less as the case may be. This part of capital is being continually transformed from a constant or unchangeable magnitude into a variable or changeable one. Therefore, it is called variable capital (Marx, 1906, pp. 232-233).

Marx describes the difference between constant capital and variable capital in the following passage:

Suppose a capitalist to employ a hundred workmen, at thirty pounds a year each, in a carpet factory. The variable capital annually laid out amounts, therefore, to 3,000 pounds. Suppose also that he discharges fifty of his workers, and employs fifty with machinery that costs him 1,500 pounds. To simplify the matter, we take no account of buildings, coal, etc. Further suppose that the raw material annually consumed costs 3,000 pounds, both before and after the change. Is any capital set free by this metamorphosis? Before the change, the total sum of 6,000 pounds consisted half of constant, and half of variable capital. After the change it consists of 4,500 constant (3,000 pounds raw material and 1,500 pounds machinery), and 1,500 variable capital. The variable capital, instead of being one half, is only one quarter of the total capital. Instead of being set free, a part of the capital is here locked up in such a way as to cease to be exchanged against labor-power; variable has been changed into constant capital (Marx, 1906, pp. 478-479).

The preceding observation by Marx on the different compositions of constant and variable capital led him to his creation of the Law of Falling Tendency of the Rate of Profit. The law states that with each new addition of capital to the constant capital there will be a reduction in the amount

of variable capital. The capitalist makes his profits from the exploitation of the laborer. So, if more capital is put into machinery, the capitalist receives less surplus-value since only labor can produce surplus-value. The increased use of machinery, therefore, leads to the fall of the rate of profits, and eventually leads to stagnation because of the loss of surplus-value upon which basis the capitalistic system rests (Marx, 1909, pp. 247-249).

If the average rate of profit for society tends to fall due to the difference in the makeup of constant and variable capital, how would stagnation be prevented according to Marx?

Marx stated in his theory of The Law of Concentration that larger industries would band together in order to obtain more surplus-value from the worker and jointly share the burden of the increasing amounts of constant capital. He also believed the stagnation caused by discrepancy of constant and variable capital might be postponed by the following methods, such as, cheapening the elements of constant capital, raising the intensity of exploitation, depression of wages below their value, relative overpopulation, and foreign trade (Marx, 1909, pp. 272-278).

Before Marx, economists were somewhat pessimistic and predicted stagnation in the long term. However, Marx and his followers left no doubt as to the future of capitalistic society.

The barriers of the capitalistic mode of production becomes apparent after our study:

1. The fact that the development of the productive powers of labor creates in the falling rate of profit a law which turns into an antagonism of this mode of production at a certain point and requires for its defeat a periodic crisis.
2. The fact the expansion or contraction of production is determined by the appropriation of unpaid labor, and by the proportion of the unpaid labor to the materialized labor in general, or to speak the language of the capitalist, is determined by profits and by the proportion of this profit to the employed capital, by a definite rate of profit, instead of being determined the relation of production to social wants, to the wants of socially developed human beings. The capitalistic mode of production, for this reason, meets with barriers at a certain scale of production which would be inadequate under different conditions. It comes to a standstill at a point determined by the production and realization of profit, not by the satisfaction of social needs (Marx, 1909, p. 303).

Answering the question of methods of preventing stagnation, Marx said "...capitalistic production is continually engaged in the attempt to overcome these imminent barriers, but it overcomes them only by means which again place the same barriers in the way in a more formidable size" (Marx, 1925, p. 293).

Marx believed that capitalistic society would come to an end when the Reserve Army of the Unemployed forced by the Law of Increasing Misery of the Proletariat arose and revolted against their oppressors, and established over themselves the Dictatorship of the Proletariat until the masses were trained to no longer need any form of government whatsoever. Without this revolution, Marx saw no actual solution to the dilemma posed by the laws of capitalistic production and the eventual stagnation of the economy.

Chapter Four: Institutional Economics on Stagnation

Institutional economics has many followers but for our purpose of analyzing the views on stagnation, we will mainly focus on the writings of Thorstein Veblen. Before continuing to our examination of Veblen's theory of stagnation in capitalistic societies, we must first examine some of the preconceptions of Institutional economics.

The economic thought of the Classical economist is based in Classical philosophy with its doctrines of 'Natural and Immutable Laws', and the Malthusian theory of population. Marxian economist's thought is founded in the idealistic philosophy of Hegel. The economic thought of Institutional economists is based on the same preconceptions of 'Instrumentalism' of John Dewey and the 'Pragmatism' of William James. In other terms, Institutional economics, Instrumentalism, Pragmatism, and Logic are all based on the doctrines of the Metaphysical Club, founded by Charles S. Pierce in the 1860s. The club was attended by William James, John Fiske, Chauncey Wright, and a few other intellectuals from Cambridge (Hofstadter, 1945, pp. 105-106).

Thorstein Veblen's theory of stagnation, which we will examine more closely, is based on a dichotomy of technology and institutions. The dichotomy in Veblen's thinking develops from his early training in Hegelian philosophy (Dorfman, 1947, pp. 40-45) and from the teachings of Charles S. Pierce (Daugert, 1950, pp. 16-25). However, this dichotomous thinking of Veblen may also be observed in John Dewey's thinking – for technology substitute education and for the imbecile institutions substitute "the quest for certainty" (Dewey, 1929).

Veblen's theory of economic stagnation of society may be best captured from his analysis of the machine process and business enterprise. Veblen defines the machine process in the following way:

In its bearing on modern life and modern business, the machine process means something more comprehensive and less external than a mere aggregate of mechanical appliances for the meditation of human labor. It means that, but it means something more than that. The civil engineer, the mechanical engineer, the navigator, the mining expert, the industrial chemist and the mineralogist, the electrician – the work of all these fall within the line of the modern machine process, as well as the work of the inventor who devises the appliances of the process and that of the mechanic who puts the inventions into effect and oversees their working. The scope of the process is larger than the machine. In those branches of industry in which the machine methods have been introduced, many agencies which are not to be classed as mechanical appliances, simply have been drawn into the process and have become integral factors in it. Chemical properties of minerals, e.g., are counted on in the carrying out of metallurgical processes with much the same certainty and calculable effect as are the motions of those mechanical appliances by whose use the minerals are handled. The sequence of the process involves both the one and the other, both the apparatus and the materials, in such intimate interaction that the process cannot be spoken of simply as an action of the apparatus upon the materials. It is not simply that the apparatus reshapes the materials: the materials reshape themselves by the help of the apparatus. Similarly, in such other processes as the refining of petroleum, oil, or sugar; in the work of the industrial chemical laboratories; in the use of wind, water, or electricity (Veblen, 1904, pp. 5-6).

Veblen goes on to define business enterprise:

The economic welfare of the community at large is best served by a facile and uninterrupted interplay of the various processes which make up the industrial system at large; but the pecuniary interests of the business men in whose hands lies the discretion in the matter are not necessarily best served by an unbroken maintenance of the industrial balance. Especially is this true as regards those greater business men whose interests are very extensive. The pecuniary operations of these latter are of large scope, and their fortunes commonly are not permanently bound up with the smooth working of a given Sub-process in the industrial system. Their fortunes are rather related to the larger conjunctures of the industrial system as a whole, the interstitial adjustments, or to conjunctures affecting large ramifications of the system. Nor is it at all uniformly to their interest to enhance the smooth working of the industrial system at large in so far as they are related to it. Gain may come to them from a given disturbance of the system whether the disturbance makes for heightened facility or for widespread hardship, very much as a speculator in grain futures may be either a bull or a bear. To the business man who aims at a differential gain arising out of interstitial adjustments or disturbances of the industrial system, it is not a material question whether his operations have an immediate furthering or hindering effect upon the system at large. The end is pecuniary gain, the means is disturbance of the industrial system, – except so far as the gain is sought by the old-fashioned method of permanent investment in some one industrial or commercial plant, a case which is for the present left on one side as not bearing on the point immediately in hand (Veblen, 1904, pp. 27-28).

Before beginning our analysis of Veblen's theory of capitalistic stagnation, we must first examine his thoughts on the business cycle for any information that may help us understand his analysis of stagnation.

Veblen attributes the business cycle to the use of loan credit. He writes:

An industrial crisis is a period of liquidation, cancelment of credits, high discount rates, falling prices and "forced sales," and shrinkage of values. It has as a sequel, both severe and lasting, a shrinkage of capitalization throughout the field affected by it. It leaves the business men collectively poorer, in terms of money value; but the property which they hold between them may not be appreciably smaller in point of physical magnitude or of mechanical efficiency than it was before the liquidation set in. It commonly also involves an appreciable curtailment of industry, more severe than lasting; but the effects which a crisis has in industry proper are commonly not commensurate with its consequences in business or with the importance attached to a crisis by the business community (Veblen, 1904, pp. 190-192).

Whereas Classical economists attribute depressions to the hand of God, Veblen explained depressions are of necessity tied to the mechanisms of a capitalistic society and that the "immediate occasion of such a crisis, then, is that there arises a practical discrepancy between the earlier effective capitalization on which the collateral has been accepted by the creditors, and the subsequent effective capitalization of the same collateral shown by quotations and sales of the securities on the market" (Veblen, 1904, p. 193).

Put in other terms, Veblen was of the opinion that depressions are "a malady of the affections. The discrepancy which discourages business men is a discrepancy between that nominal capitalization which they have set their hearts upon through habituation in the immediate past and that actual capitalizable value of their property which its current earning-capacity will warrant" (Veblen, 1904, p. 237).

Veblen held the belief that crises and depressions do not destroy the material wealth of a community, rather, only the income of the businessman.

Under the old order, industry, and even such trade as there was, was a quest of livelihood; under the new order industry is directed by the quest of profits. Formerly, therefore, times were good or bad according as the industrial processes yielded a sufficient or an insufficient output of the means of life. Latterly times are good or bad according as the process of business yields an adequate or inadequate rate of profits. The controlling end is different in the present, and the question of welfare turns on the degree of success with which this different ulterior end is achieved. Prosperity now means, primarily, business prosperity; whereas it used to mean industrial sufficiency (Veblen, 1904, p. 178).

John Maynard Keynes in his book The General Theory of Employment, Interest, and Money once said in reference to the business cycle and full employment: “I doubt that, except during war (World War I), we have had any recent experience of a boom so strong that it led to full employment” (Keynes, 1936, p. 322).

Thirty years before this statement by Keynes, Veblen had some similarly interesting remarks:

It might even be a tenable generalization, though perhaps unnecessarily broad, to say that for a couple of decades past the normal condition of industrial business has been a mild but chronic state of depression, and that any marked departure from commonplace dull times has attracted attention as a particular case calling for a particular explanation (Veblen, 1904, p. 184).

Before proceeding to the examination of Veblen’s theory of stagnation, we turn to Joseph Dorfman to summarize Veblen’s theory of the business cycle.

The scope and method of modern industry are given by the machine. The machine process implies and enforces a sweeping standardization of processes, goods, services, and consumers. Mankind, in order to get along with the machine process and reap the benefits of its efficiency, must adapt itself to its impersonal, standardized requirements. The machine process denotes a reasoned procedure as against the rule of thumb of the traditional scheme of control, where personal propensity is the dominant feature and where the industrial processes and material procedures must adapt themselves to the needs of the

big businessman. Advance in industrial efficiency is due to the comprehensive, concatenated character of the entire process, and the economic welfare of the community is best served by a facile and uninterrupted inter-play of its various parts.

But the greater gains of the modern captain are made in disturbing the delicate interstitial adjustments between plants and processes. Great profits are achieved not from productive efficiency, but from the shifts in the distribution of ownership in vendible capital or securities. The modern captain is interested not in the permanent efficiency of the industrial system or of any plant, but in the control of a segment of the system for the strategic purpose of influencing the security market for the flotation of securities, the maneuvering of a coalition or any other well-known method of manipulation. The results of his maneuvering and strategic activity is a chronic perturbation of industry, which has become the normal state of affairs. The modern captain does not create opportunities for increasing industrial efficiency, but only watches for opportunities to put his competitors in an uncomfortable position; cut-throat competition, rate wars, duplication, misdirection, wasted efforts, and even delay of improvements long after they are advisable are the price the community pays. When the game between competing business interests is played to a finish, in a coalition of the competitors under single management, then it may proceed more obviously as a conflict between the monopoly and the community. By virtue of the delicate character of the industrial process as a whole, a small apparent disturbance by the captains has a cumulative effect throughout the system far in excess of the original disturbance and is typified by such phenomena as crises and depressions. (Dorfman, 1947, pp. 225-226)

With our conclusion of Veblen's theory of the business cycle, we can now resume our examination of Veblen's theory of stagnation of the capitalistic society.

The Classical and Marxian economists, in the previous chapters, were shown to have very pessimistic views of the stationary state. However, for a truly dismal picture of a capitalistic society, you must look at the works of Veblen in which he discusses capitalistic stagnation. Veblen's discussion of stagnation takes two directions. The first is in the direction of a changed social situation and more equitable utilization of resources that are derived from the machine process. The second direction is one of a revision to barbarism, militarism, and patriotism.

Veblen develops two differing views of stagnation in his writings. In The Theory of Business Enterprise, he has hopes for the future; however, in Absentee Ownership his view is completely gloomy. In an effort to see these distinctions in Veblen's thinking, it is necessary to

examine the two books separately. First, we will examine stagnation references in The Theory of Business Enterprise and then turn our attention to Absentee Ownership.

The Classical economists viewed stagnation as an end in itself, and the Marxian economists conceived capitalistic stagnation as a phase leading to the overthrow of the system completely by the revolt of the proletariat. Keynesian economists, as we will see later, believe stagnation will be staved off by the government's manipulation of the money markets and through nationalization of national industries. Veblen, however, sees stagnation leading either to a total discontinuation of capitalism or to a maintenance of the status quo through 'force and fraud.'

Veblen believed stagnation would arise in a capitalistic society due to the business cycle and the perfection of competition, as well as from nationalism and the status system, "under the regime of a perfected machine industry and perfect business organization, with active competition throughout, it is at least probable that depression would not be seriously interrupted by any other cause." (Veblen, 1904, p. 245)

Veblen also maintained that stagnation will be the result a 'conscientious withdrawal of productive efficiency' in a machine civilization.

Depression and industrial stagnation follow only in case the pecuniary exigencies of the situation are of such a character as to affect the traffic of the business community in an inhibitory way. But business is the quest of profits, and an inhibition of this quest must touch the seat of its vital motives. Industrial depression means that the business men engaged do not see their way to derive a satisfactory gain from letting the industrial process go forward on the lines and in the volume for which the material equipment of industry is designed. It is not worth their while, and it might even work them pecuniary harm. Commonly their apprehension of the discrepancy which forbids an aggressive pursuit of industrial business is expressed by the phrase "overproduction." An alternative phrase, intended to cover the same concept, but less frequently employed, is 'underconsumption.' (Veblen, 1904, pp. 213-214)

We have pointed out that Veblen saw capitalistic society doomed for stagnation due to the following cultural lags: the business cycle, the conscientious withdrawal of productive efficiency, and from the devotion to the imbecile institutions of government, church, national sentiments, and education.

So, does Veblen see any escape from this dilemma of stagnation? Veblen sees it prevented by either of these two methods: a more equitable distribution of the goods of society, or a reversion to militarism.

The largest and most promising factor of cultural discipline – most promising as a corrective of iconoclastic vagaries – over which business principles rule is national politics. The purposes and the material effects of business politics have already been spoken of above, but in the present connection their incidental, disciplinary effects are no less important. Business interests urge an aggressive national policy and business men direct it. Such a policy is warlike as well as patriotic. The direct cultural value of a warlike business policy is unequivocal. It makes for a conservative animus on the part of the populace. During war time, and within the military organization at all times, under martial law, civil rights are in abeyance; and the more warfare and armament the more abeyance. Military training is a training in ceremonial precedence, arbitrary command, and unquestioning obedience. A military organization is essentially a servile organization. Insubordination is the deadly sin. The more consistent and the more comprehensive this military training, the more effectually will the members of the community be trained into habits of subordination and away from that growing propensity to make light of personal authority that is the chief infirmity of democracy. This applies first and most decidedly, of course, to the soldiery, but it applies only in a less degree to the rest of the population. They learn to think in warlike terms of rank, authority, and subordination, and so grow progressively more patient of encroachments upon their civil rights.

...Warlike and patriotic preoccupations fortify the barbarian virtues of subordination and prescriptive authority. Habituation to a warlike, predatory scheme of life is the strongest disciplinary factor that can be brought to counteract the vulgarization of modern life wrought by peaceful industry and the machine process, and to rehabilitate the decaying sense of status and differential dignity.

In this direction, evidently, lies the hope of a corrective for "social unrest" and similar disorders of civilized life. There can, indeed, be no serious question but that a consistent return to the ancient virtues of allegiance, piety, servility, graded dignity, class prerogative, and prescriptive authority would greatly conduce to popular content and to the facie management of affairs. Such is the promise held out by a strenuous national policy. (Veblen, 1904, pp. 392-393)

Veblen was of the belief that a return to ‘the old virtues’ of militarism and a strenuous national policy would prevent stagnation; however, even in this dismal passage he takes heart and states:

It is difficult to believe that the machine technology and the pursuit of the material sciences will be definitively superseded, for the reason, among others, that any community which loses these elements of its culture thereby loses that brute material force that gives it strength against its rivals. (Veblen, 1904, p. 400)

The preceding passages that appeared in 1904 proved Veblen’s doubts as to the lasting qualities of a capitalistic society that employed the machine process merely as an aid to increasing its income, but in 1923, these were his sentiments:

...With every further move along the lines on which the industrial arts are advancing, therefore, sabotage – that is to say the strategic unemployment at the instance of the owner-employer or of the workmen – becomes a swifter and more widely corrosive agency of miscarriage and decay.

At the same time, and in great part by help of these same technical appliances and powers, the business community is able, also in a progressive fashion to bring sound conservative business principles to bear on industry in a swifter and more comprehensive way and with a slighter margin of error. That is to say novelties will be disallowed with a freer hand and the tactical maneuvers of unemployment will gain something in frequency and amplitude; measures to suppress or disable the organization of workmen and malcontent will take on added scope, assurance, vigor, and dispatch. (Veblen, 1924, p. 421)

Once more in Absentee Ownership Veblen states, “It is conceivable that the civilized peoples might yet save themselves alive out of this impasse of their addiction to business, if it were not for their national integrity.” (Veblen, 1924, p. 422)

Uncritical devotion to the national pretensions being a meritorious habit, it is also a useful article of camouflage, a shelter for gainful enterprises and transactions which might otherwise be open to doubt, a means of avoiding unfavorable notice of procuring a profitable line of good will. (Veblen, 1924, p. 427)

Veblen finishes Absentee Ownership with the following words in reference to capitalistic stagnation:

The outlook should accordingly be that the businesslike control of the industrial system in detail should presently reach, if it has not already reached, and should speedily pass beyond that critical point of chronic derangement in the aggregate beyond which a continued pursuit of the same strategy on the same businesslike principles will result in a progressively widening margin of deficiency in the aggregate material output and a progressive shrinkage of the available means of life. (Veblen, 19224, p. 445)

In other words, capitalistic society will end either in a more equitable distribution of the goods of society or in a militaristic state as a result of stagnation. Finally, we can look the following passage from Veblen to summarize:

It seems possible to say this much, that the full dominion of business enterprise is necessarily a transitory dominion. It stands to lose in the end whether the one or the other of the two divergent cultural tendencies wins, because it is incompatible with the ascendancy of either. (Veblen, 1904, p. 400)

Chapter Five: Keynes on Stagnation

As discussed in previous chapters, Classical, Marxian, and Institutional economists all saw the future of capitalistic civilization as one of stagnation. John Stuart Mill and his followers were of the opinion that this state of stagnation would be reached in a highly advanced civilization (Mill 746-751). Marx and his followers considered this state of stagnation merely as a phase of the dialectical movement leading to a classless society. Veblen saw capitalistic society doomed for stagnation due to cultural lags such as the business cycle, the conscientious withdrawal of productive efficiency, and from the devotion to the imbecile institutions of government, church, national sentiments, and education.

John Maynard Keynes in his book The General Theory of Employment, Interest, and Money, attempted to discover methods by which capitalistic society might be saved from unemployment, depression, and eventual stagnation. In this chapter, we will examine Keynes' writing in order to point out certain postulates of the Keynesian system that will lead to capitalistic stagnation.

The theory of stagnation that arises from the doctrines of the Keynesian system can be viewed through two separate vantage points. The first is the marginal efficiency of capital and the rate of interest. Keynes on the marginal efficiency of capital and the rate of interest:

I define the marginal efficiency as being equal to the rate of discount which would make the present value of the series of annuities given by the returns expected from the capital-assets during its life just equal to its supply price. This gives it the marginal efficiencies of particular types of capital-assets. The greatest of these marginal efficiencies can then be regarded as the marginal efficiency of capital in general (Keynes, 1936, pp. 135-136).

The rate of interest is in itself nothing more than the inverse proportion between a sum of money and what can be obtained for parting with control over the money in exchange for a debt for a stated period of time (Keynes, 1936, p. 167).

The second vantage point from which we can view the theory of stagnation is the liquidity preference and the propensity to consume. Keynes also takes the liberty of defining these concepts for us:

Liquidity-preference is a potentiality of functional tendency, which fixes the quantity of money which the public will hold when the rate of interest is given so that if r is the rate of interest, M the quantity of money and L the function of liquidity preference, we have $M = L(r)$ (Keynes, 1936, p. 168).

We shall define the propensity to consume as the functional relationship X between Y_w as a given level of income in terms of wage-units, and C_w the expenditure on consumption out of that level of income so that: $C_w = X(Y_w)$ or $C = W \cdot X(Y_w)$ (Keynes, 1936, p. 90).

Keynesian economics emerged as an attempt to solve the numerous problems facing society in the days of the Great Depression of 1929-1939. Keynes' writings were revolutionary in his approach to economic problems.

Keynes believed that full employment might be reached by widening the gap between the marginal efficiency of capital and the rate of interest. As evidenced by the following passage, Keynes believed that interest was a reward for not hoarding which is in contrast to Classical economists who believed interest was a reward for saving.

It is to our best advantage to reduce the rate of interest to that point relatively to the schedule of the marginal efficiency of capital at which there is full employment. There can be no doubt that this criterion will lead to a much lower rate of interest than has ruled hitherto; and, so far as one can guess at the schedules of the marginal efficiency of capital corresponding to increasing amounts of capital, the rate of interest is likely to fall steadily, if it should be practicable to maintain conditions of more or less continuous full employment—unless, indeed, there is an excessive change in the aggregate propensity to consume (including the State).

I feel sure that the demand for capital is strictly limited in the sense that it would not be difficult to increase the stock of capital up to a point where its marginal efficiency had fallen to a very low figure. This would not mean that the use of capital instruments would

cost almost nothing, but only that the return from them would have to cover little more than their exhaustion by wastage and obsolescence together with some margin to cover risk and the exercise of skill and judgment. In short, the aggregate return from durable goods in the course of their life would, as in the case of short-lived goods, just cover their labour-costs of production plus an allowance for risk and the costs of skill and supervision.

Now, though this state of affairs would be quite compatible with some measure of individualism, yet it would mean the euthanasia of the rentier, and, consequently, the euthanasia of the cumulative oppressive power of the capitalist to exploit the scarcity value of capital. Interest to-day rewards no genuine sacrifice, any more than does the rent of land. The owner of capital can obtain interest because capital is scarce, just as the owner of land can obtain rent because land is scarce (Keynes, 1936, pp. 375-376).

The preceding quotation does not provide the entire reasoning behind Keynes' belief that full employment may be reached by lowering the rate of interest. The following quotation, however, may clear things up:

If there is some tendency to a measure of long-run uniformity in the state of liquidity-preference, there may well be some sort of rough relationship between the national income and the quantity of money required to satisfy liquidity-preference, taken as a mean over periods of pessimism and optimism together. There may be, for example, some fairly stable proportion of the national income more than which people will not readily keep in the shape of idle balances for long periods together, provided the rate of interest exceeds a certain psychological minimum; so that if the quantity of money beyond what is required in the active circulation is in excess of this proportion of the national income, there will be a tendency sooner or later for the rate of interest to fall to the neighbourhood of this minimum. The falling rate of interest will then, *cet. par.*, increase effective demand, and the increasing effective demand will reach one or more of the semi-critical points at which the wage-unit will tend to show a discontinuous rise, with a corresponding effect on prices (Keynes, 1936, pp. 306-307).

The gap that can be made to exist between the rate of interest and the marginal efficiency of capital may be manipulated by the government, according to Keynes. This is executed in order to deliver full employment and a high propensity to consume, which will in turn solve the problem of secular stagnation.

With the constant lowering of the rate of interest, the zero gap is created between the rate of interest and the marginal efficiency of capital which will stimulate investment and lead to full employment. However, it seems that this type of action will lead to a reduction in the marginal efficiency of capital to zero. If that happens as a result of lowering the rate of interest to zero, has the problem of secular stagnation been removed or only postponed for a brief period of time?

Keynes expressed his doubts about the effectiveness of this solution to stagnation and unemployment in these words, “Thus even if the rate of interest is zero, there is a strict limit to the proportion of prospective consumers’ demand which it is profitable to begin providing for in advance” (Keynes, 1936, pp. 217).

Keynes went on to state in his General Theory that monetary policy alone is not always enough to remedy an economic downturn or stagnation. This has been used as an argument for deficit spending as an answer for secular stagnation.

For my own part I am now somewhat skeptical of the success of a merely monetary policy directed towards influencing the rate of interest. I expect to see the State, which is in a position to calculate the marginal efficiency of capital-goods on long views and on the basis of the general social advantage, taking an ever greater responsibility for directly organizing investment; since it seems likely that the fluctuations in the market estimation of the marginal efficiency of different types of capital, calculated on the principles I have described above, will be too great to be offset by any practicable changes in the rate of interest (Keynes, 1936, p. 164).

Now that we have shown that the theory of stagnation is inherently a part of Keynes’ theory of monetary manipulation, we can shift our attention to the discrepancy between the propensity to consume and the propensity to save and their relation to the theory of secular stagnation.

In his General Theory, Keynes lists the following objective factors influencing the propensity to consume:

1. A change in the wage units.
2. A change in the difference between income and net income.
3. Windfall changes in capital-values not allowed for in calculating net income.
4. Changes in the rate of time-discounting.
5. Changes in fiscal policy.
6. Changes in expectations of the relation between the present and the future level of income (Keynes, 1936, pp. 91-95).

Considering these factors influencing the propensity to consume, Keynes concluded, “In a given situation the propensity to consume may be considered a fairly stable function, provided that we have eliminated changes in the wage-unit in terms of money” (Keynes, 1936, p. 95).

The propensity to consume is one of the factors that contributes to employment and to the full utilization of economic resources; therefore, if the propensity to consume remains stable or tends to fall there will be a tendency for the economy to have less than full employment and the economy will eventually stagnate. Keynes concluded from his examination of the trend in the propensity to consume and the propensity to save that,

...there has been a chronic tendency throughout human history for the propensity to save to be stronger than the inducement to invest. The weakness of the inducement to invest has been at all times the key to the economic problem. Today the explanation of the weakness of this inducement may chiefly lie in the extent of existing accumulations; whereas, formerly, risks and hazards of all kinds may have played a larger part. But the result is the same. The desire of, the individual to augment his personal wealth by abstaining from consumption has usually been stronger than the inducement to the entrepreneur to augment the national wealth by employing labour on the construction of durable assets (Keynes, 1936, pp. 347-348).

If the propensity to consume and the propensity to save are factors in full employment and the development of the economic system, and there is a tendency for saving to exceed consumption, what had prevented stagnation up to the point where Keynes wrote his General Theory? Keynes answered that in the following way:

... the frequency of war over the average of (say) each decade seems to have been sufficient, taken in conjunction with the propensity to consume, to establish a schedule of the marginal efficiency of capital which allowed a reasonably satisfactory average level of employment to be compatible with a rate of interest high enough to be psychologically acceptable to wealth-owners (Keynes, 1936, p. 307).

Keynes again stated that because of the discrepancy of the propensity to consume and the propensity to save he doubted if, “except during the war (World War I) we have had any recent experiences of a boom so strong that it led to full employment” (Keynes, 1936, p. 322).

In conclusion, our study of Keynes has shown that society will be driven into stagnation by discrepancy in the propensity to consume and the propensity to save. We also examined the relationship of the marginal efficiency of capital and the rate of interest and revealed that the government manipulation of the rate of interest may postpone stagnation for a time. However, the marginal efficiency of capital tends to fall to zero, and this in turn will lead capitalistic society into stagnation.

As we will see in the next chapter, economists from Harvard University and other schools used the General Theory of Employment, Interest, and Money during the ‘Keynesian Revolution’ as a basis for their theories of ‘The Matured Economy’. We will mostly focus on the ideas of the American economist, Alvin Hansen.

Chapter Six: Alvin Hansen and the Matured Economy

The theories of 'The Matured Economy' were first introduced during the Keynesian Revolution by various economists. We must first examine the theory and explain the basic postulates of the matured economy. Here are the basic postulates of the theory of the matured economy:

1. The declining rate of population. The decline in the birth rate according to these economists, including Alvin Hansen, means that the entrepreneur cannot find enough places in which to invest his money profitably. In turn, the economy becomes stagnant and unemployment rises.
2. The disappearance of the frontiers, with the consequential loss of investment opportunities. When there is no more land to explore or expand to, stagnation will set in.
3. The lack of new industries that will create jobs and investment opportunities. Economic growth will slow due to the lack of new business and jobs, also leading to higher unemployment (Hansen, 1938).

These were the three reasons that would ultimately lead to secular stagnation in the economy. Paul Sweezy summarizes Hansen's stagnation theory:

According to this theory, the modern developed capitalist economy has an enormous capacity to save, both because of its corporate structure and because of the very unequal distribution of personal income. But if adequate profitable investment opportunities are lacking, this saving potential translates not into real capital formation and sustained growth but into lowered income, mass unemployment, and chronic depression, a condition summed up in the term stagnation (Sweezy, 1982, p. 53).

In a presentation given by Alvin Hansen in 1939, he was attempting to draw a contrast between a cyclical period of slow growth and a structural change in the economy. Hansen was of the mindset that the world at that time was not experiencing a normal downturn in the business cycle, but rather, we were entering a new era of much slower growth. He stated, “We are passing, so to speak, over a divide which separates the great era of growth and expansion of the nineteenth century from an era which no man, unwilling to embark on pure conjecture, can yet characterize with clarity or precision.” The Great Depression, in the eyes of Hansen, was something that might last indefinitely because of structural changes (Hansen, 1939).

The first part of Hansen’s theory we will look at is the idea of declining population growth. He believed the slower population growth would lead to slower economic growth. Here are Hansen’s thoughts on the effect of population growth:

Now the rate of population growth must necessarily play an important role in determining the character of the output; in other words, the composition of the flow of final goods. Thus a rapidly growing population will demand a much larger per capita volume of new residential building construction than will a stationary population. A stationary population with its larger proportion of old people may perhaps demand more personal services; and the composition of consumer demand will have an important influence on the quantity of capital required. The demand for housing calls for large capital outlays, while the demand for personal services can be met without making large investment expenditures. It is therefore not unlikely that a shift from a rapidly growing population to a stationary or declining one may so alter the composition of the final flow of consumption goods that the ratio of capital to output as a whole will tend to decline (Hansen, 1939, p. 7).

Hansen believed that economists should resort to the ideas of Adam Smith on population growth as opposed to the more pessimistic views of Thomas Malthus and David Ricardo. Smith thought population growth led to further growth and expansion. Ricardo and Malthus believed that rapid population growth would likely lead to the stagnation of the capitalistic society.

Adam Smith regarded growth of population as at once a consequence and a cause of economic progress. Increasing division of labor would, he argued, bring about greater

productivity, and this would furnish an enlarged revenue and stock, from which would flow an enlarged wages fund, an increased demand for labor, higher wages, and so economic conditions favorable for population growth. Now a growing population, by widening the market and by fostering inventiveness, in turn facilitated, he thought, division of labor and so the production of wealth. Thus he arrived at an optimistic conclusion. Population growth, he held, stimulated progress and this in turn stimulated further growth and expansion. In contrast, the pessimistic analyses of Malthus and Ricardo stressed the limitation of natural resources and the danger of an increasing population's pressing down the margin of cultivation to a point at which real income would be reduced to a bare subsistence level. In this static analysis the more dynamic approach of Adam Smith was quite forgotten. If we wish to get a clear insight into the economic consequences of the current decline in population growth, it is necessary to return to the suggestion of Adam Smith and to explore more fully the causal inter-connection between economic progress, capital formation and population growth (Hansen, 1939, pp. 2-3).

Hansen believed that a considerable amount of economic growth could be attributed to the expansion to the western frontier. The development of new territories was certainly intertwined with population growth. A big proportion of capital formation in the United States went into the western frontier in the nineteenth century. Hansen concluded that, "the opening of new territory and the growth of population were together responsible for a very large fraction-possibly somewhere near one-half-of the total volume of new capital formation in the nineteenth century" (Hansen, 1939, p. 9).

Hansen revealed that outlets for further investment in new territories were rapidly diminishing. One would have to look somewhere else for new investment opportunities. Joseph Schumpeter, another American economist, labeled Hansen's theory the "theory of vanishing investment opportunities" (Sweezy, 1982, p. 53).

Hansen thought it was up to the progress of technology to lead bring full employment and more private investment. But would it be enough to offset the declining growth in population which hurts economic growth? Hansen wrote,

Thus the outlets for new investment are rapidly narrowing down to those created by the progress of technology. To be sure, the progress of technology itself played in the nineteenth century a decisive role in the opening of new territory and as a stimulus to population growth. But while technology can facilitate the opening of new territory, it cannot create a new world or make the old one bigger than it is. And while the advance of science, by reducing the death rate, was a major cause of the vast nineteenth-century increase in population, no important further gains in this direction can possibly offset the prevailing low birth rate. Thus the further progress of science can operate to open investment outlets only through its direct influence on the technique of production (Hansen, 1939, pp. 9-10).

Hansen said there was no greater mistake in the analysis of economic trends than those which finds that the advance of technology was a major cause of unemployment. He said that you cannot discount the problem of technological unemployment which may be intensified as the importance of capital-saving increases. However, you cannot disregard the type of innovations that lead to new industries and which thereby creates new outlets for investment. Hansen said, "What we need is not a slowing down in the progress of science and technology, but rather an acceleration of that rate" (Hansen, 1939, p. 10).

The most important thing for the economy, according to Hansen, is the development of new industries. With the decreasing expansion into new frontiers, it was up to technological advancements to fill the void. New industries such as railroads and the automobile, contributed greatly to economic growth. Also contributing to the growth was the construction of public roads for these new automobiles. When these industries mature, however, new industries must emerge to continue economic growth or the economy will inevitably stagnate.

And when a revolutionary new industry like the railroad or the automobile, after having initiated in its youth a powerful upwards urge of investment activity, reaches maturity and ceases to grow, as all industries finally must, the whole economy must experience a profound stagnation, unless indeed new developments take its place. It is not enough that a mature industry continues its activity at a high level on a horizontal plane (Hansen, 1939, pp. 10-11).

Hansen said, “It is the *cessation of growth* which is disastrous.” After strong periods of growth from particular industries, they will mature and growth will slow. When giant new industries have spent their force, it can take a long time for something of equal magnitude to emerge. Hansen pointed out that this phenomenon was taking place in the 1930s as no new industries were emerging (Hansen, 1939, p. 11).

It was that failure of new industries emerging that was causing the slow or negative economic growth along with unemployment.

But a full-fledged recovery calls for something more than the mere expenditure of depreciation allowances. It requires a large outlay on new investment, and this awaits the development of great new industries and new techniques. But such new developments are not currently available in adequate volume. It is my growing conviction that the combined effect of the decline in population growth, together with the failure of any really important innovations of a magnitude sufficient to absorb large capital outlays, weighs very heavily as an explanation for the failure of the recent recovery to reach full employment (Hansen, 1939, p. 11).

In the absence of adequate technological progress, what policies could be used in order to stave off stagnation and maintain full employment? Hansen had a few different ideas, which are generally agreed upon among Keynesian economists. Hansen believed that lowering the rate of taxes on workers could strengthen consumption by directing more of their income towards consumption rather to the government. Public investment is another tactic that can be used to combat unemployment and slowing growth. Investments made in human and natural resources and in consumers’ capital goods will serve the physical, recreational, and cultural needs of community as a whole. Hansen warned that such programs, whether financed by taxation or borrowing, may adversely affect the system of free enterprise.

Can a rising public debt owned internally be serviced by a scheme of taxation which will not adversely affect the marginal return on new investment or the marginal cost of borrowing? Can any tax system, designed to increase the propensity to consume by means

of a drastic change in income distribution, be devised which will not progressively encroach on private investment? (Hansen, 1939, p. 12).

Public spending is the easiest of all recovery methods, and therein lies its danger. If it is carried too far, we neglect to attack those specific maladjustments without the removal of which we cannot attain a workable cost-price structure, and therefore we fail to achieve the otherwise available flow of private investment (Hansen, 1939, p. 14).

Hansen admitted that this problem of secular stagnation was quite difficult and there were no definitive solutions. He said, “There are no easy answers to the problems that confront us. And because this is true, economists will not perform their function if they fail to illustrate the rapidly shifting course of economic development, and through such neglect unwittingly contribute to a dangerous lag in adjustments to change.”

Chapter Seven: Current Debate on Secular Stagnation

In November 2013, Lawrence Summers, former Treasury Secretary, delivered a speech to the International Monetary Fund at a conference dedicated to crises of yesterday and today. In his speech, Summers revived the idea of secular stagnation. Secular stagnation had not been talked about in mainstream economic circles in decades. Since the conference, Summers has expanded on this idea through other speeches and various opinion pieces in publications. Some economists have come to his defense and others have criticized his outlook.

Lawrence Summers on Secular Stagnation

Since the financial crisis of 2007-2008, the recovery has been fairly weak with slow economic growth and an unemployment rate that has only recently fallen to near normal levels. During the current recovery, real GDP growth for the six years following the end of the recession in 2009 has only averaged 2.02% quarterly. The rate of growth during recoveries or non-recession periods has steadily declined over the past thirty years. The recession of 1981-82 was followed by a six-year average real GDP growth of 4.56%. The recovery after the 1990-91 recession seen an average of 3.02% real GDP growth from 1991-1997. The recovery following the tech boom of the late 1990s had an average of 2.70% real GDP growth rate for six years following the end of the recession in 2002 (U.S. Bureau of Economic Analysis) There is a downward trend for economic growth post-recovery over the past three decades. The 1981-82 recession is the best comparison to the most recent recession since the decline in GDP is similar and unemployment reached nearly 11%. Growth following the 1981-82 recession far outpaced our current recovery.

Aside from economic growth, employment statistics have been difficult to get back to normal levels. The unemployment rate is now around 5% but other employment statistics such as

the employment-population ratio are still high. That number stands below 60%, which means over 40% of the population is not working. Before the downturn, the ratio stood above 63%. (Federal Reserve Bank of St. Louis)

These factors caused Lawrence Summers and others to invoke the theory of secular stagnation once again. Summers raised the idea that, “the American and global economies could not rely on normal market mechanisms to assure full employment and strong growth without sustained unconventional policy support.” His worries stemmed from a few different items. First, despite financial repair largely taking place five years ago, the recovery has only kept up with population growth and normal productivity growth in the United States. It’s even worse in other industrialized countries. Second, unsustainable bubbles and loose credit standards seemed to only create moderate economic growth. Third, short-term interest rates are severely constrained by zero lower bound and there is little room for further reduction which means real interest rates may not be able to fall far enough to spur enough investment to lead to full employment. Fourth, in this type of situation falling wages and prices or inflation that is below expectations is likely to worsen economic performance by encouraging consumers and investors to delay spending and to redistribute income and wealth from higher spending debtors to lower spending creditors (Summers, 2013).

At a policy conference for the National Association for Business Economics, Summers posed the question, “Can we identify any sustained stretch during which the economy grew satisfactorily with conditions that were financially sustainable?” Summers looked at various economic indicators during the recovery and revealed that the recovery itself was very weak as compared to past recoveries, which tended to be quite strong.

The record of growth for the last five years is disturbing, but I think that is not the whole of what should concern us. It is true that prior to the downturn in 2007, through the period from, say, 2002 until 2007, the economy grew at a satisfactory rate. Note that, there is no clear evidence of overheating. Inflation did not accelerate in any substantial way. But the economy did grow at a satisfactory rate, and did certainly achieve satisfactory levels of capacity utilization and employment.

Did it do so in a sustainable way? I would suggest not. It is now clear that the increase in house prices was associated with an unsustainable upward movement in the share of GDP devoted to residential investment. And this made possible a substantial increase in the debt-to-income ratio for households, which has been reversed only to a limited extent.

It is fair to say that critiques of macroeconomic policy during this period, almost without exception, suggest that prudential policy was insufficiently prudent, that fiscal policy was excessively expansive, and that monetary policy was excessively loose (Summers, 2014, pp. 66-67).

Summers goes on to explain in speech at the NABE policy conference that the data is not kind to industrial countries over the last fifteen years. The future does not look bright for those countries to maintain full employment and sustain growth.

In sum, I would suggest to you that the record of industrial countries over the last 15 years is profoundly discouraging as to the prospect of maintaining substantial growth with financial stability. Why is this the case? I would suggest that in understanding this phenomenon, it is useful at the outset to consider the possibility that changes in the structure of the economy have led to a significant shift in the natural balance between savings and investment, causing a decline in the equilibrium or normal real rate of interest that is associated with full employment (Summers, 2014, p. 69).

Summers also speaks of the decline in the equilibrium real rate of interest. He ponders if it is a plausible hypothesis currently:

Let us imagine, as a hypothesis, that this decline in the equilibrium real rate of interest has taken place. What would one expect to see? One would expect increasing difficulty, particularly in the down phase of the cycle, in achieving full employment and strong growth because of the constraints associated with the zero lower bound on interest rates. One would expect that, as a normal matter, real interest rates would be lower. With very low real interest rates and with low inflation, this also means very low nominal interest rates, so one would expect increasing risk-seeking by investors. As such, one would expect greater reliance on Ponzi finance and increased financial instability (Summers, 2014, p. 69).

There are six different reasons why Summers believes this hypothesis is reasonable for today's situation.

First he says is a decrease in demand for debt-financed investment. He says it can mostly be attributed to the changing character of productive economic activity. Capital investment is not as necessary as it once was in the past due to technological advances. The reduced demand for investment will lead to changes for equilibrium levels of interest rates.

Secondly, Summers invokes Alvin Hansen in relation to the declining rate of population growth. The labor force of the United States will grow at a much slower pace the next two decades than it has over the last two decades.

Third, changes in the distribution of income, both between labor income and capital income and between the wealthy and those with little wealth, have operated to raise the propensity to save, as have increases in corporate-retained earnings. Reduced investment demand and an increased propensity to save work in the direction of a lower equilibrium real interest rate.

Fourth, there has been a shift downward in the relative price of capital equipment. The cheaper capital goods mean that investment goods can be completed with less borrowing which reduces the propensity for investment.

Although Summers does not focus on this point too much, he says there is a legitimate argument that what matters in an economy is after-tax, rather than pre-tax, real interest rates, and the consequence of disinflation is that for any given after-tax real interest rate, the pretax real interest rate now needs to be lower than before.

Finally, there has been plenty of global moves to accumulate central bank reserves. Most of those reserves are in the form of the safe assets, such as U.S. Treasuries. Each of these factors has operated to reduce natural or equilibrium real interest rates (Summers, 2014, pp. 70-71).

So if this view is accepted as reality, what are the possible responses according to Summers? He gives us three responses: (1) Stay patient, (2) Reduce the real rate of interest, and (3) Raise demand (Summers, 2014, pp. 71-73).

The response of being patient is one that Japan has followed for many years according to Summers. He also states that the United States has essentially pursued this strategy for the last three or four years. Policy has limited impact. Summers says we are facing an inverse Say's Law. Say's Law is where supply creates its own demand but currently, we are observing that lack of demand creates its own lack of supply (Summers, p. 71).

The second response Summers suggests is to reduce the actual rate of interest. If the natural rate of interest has declined, then logically, it is appropriate to lower the actual rate of interest to permit adequate economic growth. Summers believes this is a better response than no response; however, he is skeptical that rates that stay at or below zero for a substantial time could lead to financial bubbles.

Finally, Summers believes that raising demand through fiscal policy is a proper response to secular stagnation.

The preferable strategy, I would argue, is to raise the level of demand at any given rate of interest—raising the level of output consistent with an increased level of equilibrium rates and mitigating the various risks associated with low interest rates that I have described. How might that be done? It seems to me there are a variety of plausible approaches, and economists will differ on their relative efficacy. Anything that stimulates demand will operate in a positive direction from this perspective (Summers, 2014, pp. 72).

There is some criticism that expansionary fiscal policy may not be possible because the government cannot continue to expand its debt indefinitely. Summers responds, “As long as a public investment yields a positive return it will generate enough revenue to service the associated debt.” He also adds the effect will be magnified if there are any Keynesian fiscal stimulus effects of the project or if there are any hysteresis effects. The October 2014 IMF World Economic Outlook even suggests that public investments in countries where interest rates are near the zero lower bound are likely to significantly reduce debt-to-GDP ratios (Summers, 2015).

Ben Bernanke, a critic of Summers’ position on secular stagnation summarizes it quite well in an article from March 2015:

Hansen proved quite wrong, of course, failing to anticipate the postwar economic boom (including both strong population growth—the baby boom—and rapid technological progress). However, Summers thinks that Hansen’s prediction was not wrong, just premature. For a number of reasons—including the contemporary decline in population growth, the reduced capital intensity of our leading industries (think Facebook versus steel-making), and the falling relative prices of capital goods—Larry sees Hansen’s prediction of limited investment in new capital goods and an economy that chronically fails to reach full employment as relevant today. If the returns to capital today are very low, then the real interest rate needed to achieve full employment (the equilibrium real interest rate) will likely also be very low, possibly negative. The recent pattern of slow economic growth, low inflation, and low real interest rates motivates and is consistent with the secular stagnation hypothesis.

Notice, by the way, that the secular stagnation story is about inadequate aggregate demand, not aggregate supply. Even if the economy’s potential output is growing, the Hansen-Summers hypothesis holds that depressed investment and consumption spending will prevent the economy from reaching that potential, except perhaps when a financial bubble (like the housing bubble of the 2000s) provides an additional push to spending. However, Summers argues that secular stagnation will ultimately reduce aggregate supply as well, as growth in the economy’s productive capacity is restrained by slow rates of capital formation and by the loss of workers’ skills caused by long-term unemployment (Bernanke, 2015).

Bernanke's Response to Summers

The main opponent of Lawrence Summers on the topic of secular stagnation was Ben Bernanke. The two economists exchanged ideas back forth through a series of blog posts. Bernanke had doubts if secular stagnation is actually taking place and what the proper solutions are if we are experiencing it.

Bernanke denies that the United States currently faces secular stagnation for a few different reasons, which goes beyond the fact that the U.S. economy is on its way to full employment. First, he states that if real interest rates are consistently as low as negative 2 percent it is hard to believe that there would be a permanent lack of profitable investment opportunities. As Paul Samuelson once taught him, if real interest rates were expected to be negative indefinitely, almost any investment is profitable. Therefore, it is hard to imagine that the real rate can be negative for an extended period.

Second, Bernanke agrees with another recent critique of secular stagnation by Jim Hamilton, Ethan Harris, Jan Hatzius, and Kenneth West. They have reservations with Summers' claim that we have not experienced full employment during the past several decades without the presence of a financial bubble. They reveal that the bubble in tech stocks came very late in the boom of the 1990s, and they also provide estimates to show the positive effects of the housing bubble of the 2000s on consumer demand were largely offset by other special factors, including the negative effects of the dramatic increase in world oil prices and the drain on demand created by a trade deficit equal to six percent of U.S. output. The economists argue that the slow economic growth and higher unemployment is not likely due to secular stagnation. Rather, it is due to temporary "headwinds" that are already in the process of dissipating. Bernanke, during his time as Fed chairman frequently spoke of these "headwinds" arising from the aftermath of the financial

crisis on credit conditions. The slow recovery of housing and restrictive fiscal policies at both the federal, state, and local levels also played a part.

Finally, Bernanke's biggest gripe with Summers' analysis is the lack of attention to the international dimension. Summers mostly focuses on factors affecting domestic capital investment and household spending. Bernanke, however, has said that all else equal, the availability of profitable capital investments throughout the rest of the world should help defeat secular stagnation back in the United States. Bernanke explains, "The foreign exchange value of the dollar is one channel through which this could work: If U.S. households and firms invest abroad, the resulting outflows of financial capital would be expected to weaken the dollar, which in turn would promote U.S. exports." The increased exports would then raise production and employment in the United States, helping the economy reach full employment. Therefore, in an open economy, secular stagnation requires that returns to capital investment must be permanently low everywhere, not just in the home economy (Bernanke, 2015).

A Failed Growth Economy

Economist Kent Kritgaard has a different take on the secular stagnation debate. He believes that the growth-dominated view of economies is failing us. Growth-dominated economies, including the United States, have three sets of limits. First, the internal limits are found in the dynamics of capital accumulation, specifically referring to investment. When these limits are reached, the economy will stagnate, either cyclically or long-term. The second sets of limits are biophysical in nature. The limit of peak oil and human effects on climate change. This include mass extinction, acidification of the oceans, and the increasing ecological footprint across the board. Lastly, we have the limits of the political process. Post World War II brought on a growth coalition, whose political agenda required more and more economic growth to acquire more for their constituents. As the capacity of growth lessens so does one's ability to grow out of social dilemmas. (Kritgaard, 2010)

Kritgaard goes after mainstream Neoclassical and Keynesian views by explaining that they are unable to understand their own limits. He states, "neither the neoclassical nor Keynesian varieties of mainstream economics are capable of analyzing adequately the historical conjecture off the internal and biophysical limits. Instead, he says to look to ecological economics and understand that the mainstream view of growth held by both Lawrence Summers and Ben Bernanke is incorrect. He summarizes:

The time is coming when we must begin to transcend the mere critique of mainstream economics, and concentrate on building anew. The fundamental dilemma of the failed growth economy: that growth is simultaneously too fast and too slow, cannot be addressed adequately in the context of a set of institutional arrangements that rely on economic growth to meet basic human needs of employment and freedom from poverty. We must find theories that are consistent with the basic laws of science and do not sacrifice human dignity to a failed system in which a reduction in economic growth translates into stagnation and unemployment. One can find a hope for a sustainable future only in degrowth economics (Kritgaard, 2010)

Kritgaard states that the idea that a material economy could continue to grow forever in a finite and non-growing biophysical environment is “absurd”. He calls on a new set of theories to account for the rapidly approaching biophysical constraints since the mainstream theories lack this ability.

Chapter Eight: Concluding Remarks

The idea of a stagnant economy has been with us for centuries. It started with the followers of Adam Smith in the Classical school. The theories were developed from Thomas Malthus' theory on population by John Stuart Mill and David Ricardo. The Malthusian theory of population explained that food supply would be unable to keep up with population growth in the long-term. Both Mill and Ricardo also thought the Law of Diminishing Returns would also lead to stagnation. This law says that as additional amounts of capital and labor are added to production past its optimum point, profits will continue to decrease until profit essentially falls to zero. Ricardo also believed that without improved technology, the economy would stagnate. However, he also argued that increased technology will only prevent stagnation for a brief period of time. Lastly, Ricardo thought the discrepancy between fixed and circulating capital also led to stagnant society.

Next, Karl Marx developed his own view on a stagnating economy. Marx had a very pessimistic view of capitalism. Marx and his followers believed the economy would eventually stagnate and create misery among most people. Stagnation would occur due to the falling rate of profit which Marx describes in great detail. The theory says that with each addition of capital to the constant capital, there will be a reduction in the amount of variable capital. The capitalist derives his profits from the exploitation of the laborer. An increased capital investment in machinery would lead to the fall of profits and eventually to stagnation because of the loss of surplus-value.

Thorstein Veblen had a very pessimistic outlook on capitalistic society also. Stagnation, according to Veblen would arise due to the business cycle and the perfection of competition. Additionally, nationalism and the status system would play a role in a stagnation economy. Veblen

maintained that stagnation would be the result of a 'conscientious withdrawal of productive efficiency' in a machine civilization. He predicted society will end in militaristic state as a result of stagnation or, there will be a more equitable distribution of goods.

John Maynard Keynes' work in the General Theory led to further theories developed on stagnation. But, Keynes left us with some of his own thoughts on the topic. Society would be driven into stagnation by the discrepancy in the propensity to consume and the propensity to save. Also, the relationship of the marginal efficiency of capital and the rate of interest revealed government manipulation of interest rates may postpone stagnation for some time. However, as the marginal efficiency of capital tends to fall to zero, this will lead to capitalistic society into stagnation.

Alvin Hansen developed the concept of secular stagnation and the matured economy. The matured economy occurs due to a declining rate in population, the disappearance of new frontiers, and the lack of new industries that will create jobs and investment opportunities. Hansen admitted to not having concrete solutions to stagnation but his view on the result of stagnation was more positive than previous economists before him. He believed that action can be taken by government, such as lowering taxes on workers and public investments to lessen the negative impacts of stagnation.

Finally, Lawrence Summers has recently revived Hansen's theory due to current economic conditions here in the United States and in other industrialized countries. Summers points to the slow economic growth and higher unemployment rates despite record low interest rates as evidence of a stagnating economy.

Most economists tend to disagree with the idea that secular stagnation is happening now because we have been here before. Hansen predicted that economy would be in stagnation permanently back in the 1930s into the 1940s. Those fears were revived briefly in the 1970s when stagflation was taking place in the United States. But, just as it did after the Great Depression, the economy recovered. So, there is no reason to believe that the economy won't bounce back like it always has.

A study of the various theories on stagnation and current conditions reveals that there is a chance we will face secular stagnation in the years to come. As Summers believes, Hansen's theory has not been proven wrong, it has just been put on hold. The baby boom after World War II only delayed secular stagnation. The declining rate of population and the lack of capital investment is observable in today's world. Weak economic growth has been the norm for decades.

If secular stagnation is taking place, each school of economics in which we analyzed sees different outcomes. Marx sees the overthrow of capitalism as the next step. Veblen predicted a militaristic state. Keynesians, such as Hansen say that stimulative policies can be enacted to combat stagnation but may not be permanent. Lawrence Summers and Ben Bernanke, both New Keynesians mostly believe there are remedies to the problem. Kent Kritgaard says we need a whole new approach to the idea of growth as he rejects the mainstream views that growth is infinite even in a finite biophysical environment.

The prospect that secular stagnation has set in has enormous consequences. Society must adapt to a world of little to no growth. There is not unlimited growth in this case, as many economists believe. The market cannot correct such a situation. I would suggest to economists to think outside of their normal economic theory and analyze other heterodox views. Heterodox views, such as Marxian, Institutionalist, Ecological, and Post-Keynesian may provide greater

insight into this phenomenon than the Neoclassical and New Keynesian mainstream schools. Those schools are limited in scope because of the limitations of their theory. Their theory requires many assumptions, such as consumer rationality, perfect competition, and flexible prices and wages that just cannot be replicated in this type of economy. The mainstream views of economic growth may not be possible forever.

It would be wonderful to be able to say that the United States economy along with other industrialized nations such as Japan and Germany will experience strong growth and reach full employment. However, conditions may be falling in place where stagnation finally sets in. The prevailing low rates of interest seem to be ineffective and it's virtually impossible for them to go any lower. Alvin Hansen's theory seems to have merit to it once again and other early economists seemed to be ahead of their time as well. We cannot ignore the possibility of a stationary state. Instead, we must learn to adapt or change the path we are on. This begins by breaking away from mainstream economic thinking and exploring all avenues for explanation. Secular stagnation may already be a reality.

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