

## **KEYNES AND THE REFORM OF THE CAPITALIST SOCIAL ORDER**

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*Abstract.* The ideas of Keynes have been appropriated by the political left in recent years. The condemnation of Keynes that was characteristic of critics speaking for the extreme right has become mainstream with the takeover of macroeconomic theory by schools like New Classical economics. But how radical Keynes really was? He pointedly distanced himself out of the Marxist left. However, he saw himself as a radical reformer and never missed an opportunity to advance proposals to change capitalism to produce sustained full employment and to promote some redistribution of income and wealth. The paper discusses two of these opportunities, the first related to the debate around *How to Pay for the War* and the second around the Beveridge Plan.

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## KEYNES AND THE REFORM OF CAPITALIST SOCIAL ORDER\*

### *1. Introduction*

Keynes's voice today is only heard among left wing or heterodox economists. Critics of the free markets ideology find in Keynes not only a precise analysis of the operation of a capitalist economy but also an inspiring list of policies designed to improve it substantially. Even Marxist economists are re-reading and reinterpreting Keynes's writings trying to build bridges between the two schools, attracted mainly by his views on money and finance and the instability they may cause.

To some extent, the adoption of Keynes by the left is a result of the political repositioning that has taken place all over the world since the 1980s. In fact, the overall political scene has moved so much to the right, particularly after the tenures of Mrs. Thatcher in the United Kingdom and Mr Reagan in the United States, that much of what passed as center in the past ended up "repositioned" to the left. It may be difficult for many to remember that Keynesianism, in the sense of active promotion of output and employment stability by the government, was actually the *mainstream* until the 1970s.<sup>1</sup> In the UK, Keynesianism in this sense was practiced by the Conservative as well as the Labour Party until Mrs Thatcher came to power. In that period, practically only the right-wing lunatic

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<sup>1</sup> We refer here to Keynesianism as an ideology, that is, as the set of beliefs based on the notion that the government was responsible for seeking and maintaining full employment. We are *not* referring to Keynesian economic theory nor to any development of this theory.

fringe would seriously condemn Keynes as a subversive left winger.<sup>2</sup> Today, in contrast, even a few nominally left wing leaders seem to judge Keynes a dangerous thinker.

Keynes's political views, in the widest sense, are in fact difficult to classify.<sup>3</sup> He publicly identified himself as an elitist but he also strongly believed in the powers of persuasion to convince voters to support the best policies within a democratic regime. He was a reformer by temperament, concocting continuously new schemes to address and to solve the most important problems of his time. He was friendly to social change, the search for improvement of living conditions for all and for active intervention of the State in the economy, although in ways that were, at his time, rather unconventional (some, arguably, still are). In all of his writings, one finds a permanent concern with the damaging influence of privilege on the legitimacy of the social order. In fact, he was concerned all the time with the legitimacy as well as with the efficiency of modern social, political and economic arrangements. On the other hand, if it is true that Keynes considered that modern capitalism had made free market ideologies obsolete he also rejected the radical alternatives presented by left wing reformers and Marxist revolutionaries. His vision of the future actually would preserve much of what existed while eliminating "the objectionable features of capitalism".<sup>4</sup>

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<sup>2</sup> It is interesting to observe that some of those lunatic right wingers became, in the new scenario, respected members of the new mainstream.

<sup>3</sup> Schumpeter may very well have been right when he observed that "Nobody could ever have talked to Keynes for an hour without discovering that he was the most unpolitical of men. ... Party meant little or nothing to him. He was ready to co-operate with anyone who offered support for a recommendation of his and to forget any past passage of arms. But he was not ready to co-operate with anyone on any other terms, let alone to accept anyone's leadership. His loyalties were loyalties to measures, not loyalties to individuals or groups. And still less than a respecter of persons was he a respecter of creeds of ideologies or flags." Schumpeter (1947), p. 75.

<sup>4</sup> Keynes (1964), p. 221.

In his works after *The General Theory*, Keynes repeatedly expressed concern with income concentration and advanced proposals to drastically reduce it. Many interpreters of his ideas, friend and foe alike, saw this concern as evidence of a more leftist personal bias than had been acknowledged in the past.

A notable dissident voice is Skidelsky's. In the third volume of his biography of Keynes, Skidelsky stressed his view that Keynes was not an equalitarian and that many of his proposals that could be so construed were in fact instrumental to achieve something else.<sup>5</sup> For Skidelsky, Keynes was a nationalist rather than a socialist.<sup>6</sup>

Keynes's views cannot be fitted easily in any existing political scheme. As it is often the case, one has to be careful to disentangle the implications of his theory from personal preferences that may or may not be compatible with the theory.<sup>7</sup> One can make the case, however, that Keynes's theory has reformist implications that are independent even from the author's own inclinations, which were also undoubtedly progressive, as we will try to show. In fact, it is an *implication* of his macroeconomic theory that income and wealth redistribution should be pursued, not only because it is socially fair but because it is *efficient*. The connection between income distribution and propensity to consume is a key

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<sup>5</sup> "Keynes's incuriosity about this battle [around the Beveridge Plan] is itself curious. The truth seems to be that he was not interested in social policy as such, and never attended to it. The sole question in his mind was whether the Exchequer could 'afford' Beveridge." (Skidelsky, 2000, pp. 269/270).

<sup>6</sup> Schumpeter agrees with Skidelsky on this: "... he was fervently patriotic – of a patriotism which was indeed quite untinged by vulgarity but was so genuine as to be subconscious and therefore all the more powerful to impart a bias to his thought and to exclude full understanding of foreign (also American) viewpoints, conditions, interests, and especially creeds." (Schumpeter, 1947, p. 85)

<sup>7</sup> One has to be especially careful to avoid making superficial associations such as that orthodox economists are, *ipso facto*, conservative, while non-orthodox are, for the same reason, progressive. There are plenty of politically progressive neoclassical economists, from Walras and Wicksell to Tobin, Arrow and Stiglitz. The converse is also true.

building block of Keynes's model and it is the key to understand the reformist implications of *The General Theory*.

To illustrate this point in this paper, we selected two important reform debates in which Keynes was personally involved, the first around his proposals to finance the British war effort, and the second around the Beveridge Plan. We begin by examining Keynes's mature attitude with respect to social reform. Section 3 presents some of his views about the traditional left, particularly the Marxist left. Sections 4 and 5 concern the two reformist initiatives mentioned above. Section 6 concludes the paper.

## 2. Keynes and the Reform of Capitalism

In an often-quoted letter to G.B. Shaw shortly before the publication of *The General Theory*<sup>8</sup>, Keynes stated that he expected the book to revolutionize “the way the world thinks about economic problems”. In a much less widely noted passage of that letter, Keynes states that with that work he expected to make obsolete the conflictive basis of Ricardian economics.<sup>9</sup> This quotation encapsulates an important dimension of Keynes's political view of capitalism. In a nutshell, Keynes seemed to consider that the distributive conflict that had been at the heart of social tensions in capitalist economies (and inspired some of the most radical political movements in modern History) was much less

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<sup>8</sup> I refer, of course, to Keynes's *The General Theory of Employment, Interest and Money*. In the rest of this paper, generic references to the book will identify it simply as *The General Theory*. When taking quotations or making specific references to the work, it will be referred as Keynes (1964).

<sup>9</sup> The letter is somewhat enigmatic. Keynes writes that, as a result of *The General Theory*, “there will be a great change, and, in particular, the Ricardian foundations of Marxism will be knocked away.” (CWJMK, 28, p. 42)

important than the inability of these economies to explore their full potential. If these economies could be made to produce at their full potential, *all* incomes could rise, profits *as well as* wages. The conflictive basis of Ricardian economics resided in its assumption of Say's Law, that is, that capitalist economies were, as a rule, operating at their full potential. If that assumption was correct, workers could only increase their incomes if they were capable of reducing profits, since total output was given. Keynes believed that, with *The General Theory*, he would be able to demonstrate that output could be kept *permanently* at much higher levels than what was known then, improving everybody's living conditions or allowing rising incomes for given social groups without having to reduce any other groups' real incomes. In fact, he believed that the economy could maintain boom conditions, encouraging investment to the point where scarcity of capital itself could disappear and, technically, capitalism as such could be disposed of.<sup>10</sup>

If this interpretation is correct, *enlightened* economic policy itself would work as *social reform*, and this seems precisely the way Keynes approached the question of the choice of economic policies that would be implied by his theory. As he put it in *The General Theory*:

“Thus the remedy for the boom is not a higher rate of interest but a lower rate of interest. For that many enable the so-called boom to last. *The right remedy for the trade cycle is*

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<sup>10</sup> “For the only reason why an asset offers a prospect of yielding during its life services having an aggregate value greater than its initial supply price is because it is *scarce*; ... If capital becomes less scarce, the excess yield will diminish, without its having become less productive – at least in the physical sense.” (Keynes, 1964, p. 213, emphasis in the original). “If I am right in supposing it to be comparatively easy to make capital goods so abundant that the marginal efficiency of capital is zero, this may be the most sensible way of getting rid of many of the objectionable features of capitalism.” (idem, p. 221)

*not to be found in abolishing booms and thus keeping us permanently in a semi-slump; but in abolishing slumps and thus keeping us permanently in a quasi-boom.*" (Keynes, 1964, p. 322, emphases added)

Again, in the last chapter of *The General Theory*, Keynes identifies the two main problems of capitalist economies as being an excessive degree of income concentration and the inability of these economies to maintain full employment of their resources.<sup>11</sup>

According to Keynes, solving the first problem would not be so hard. First, because, as Skidelsky rightly notes, Keynes was *not* an equalitarian. It was not concentration as such that was the problem, but *excessive* concentration.<sup>12</sup> Excessive with respect to what? Keynes, as Schumpeter, accepted that a certain degree of inequality was socially functional, in the sense that it induced behaviors that resulted in a greater good for society as a whole. Thus, it was acceptable that entrepreneurs willing to face the uncertainties of investment and innovation should be properly rewarded. Society benefited from the larger accumulation of capital and from the increase in productivity.<sup>13,14</sup> However,

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<sup>11</sup> "The outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes." (Keynes, 1964, p. 372)

<sup>12</sup> "For my own part, I believe that there is social and psychological justification for significant inequalities of incomes and wealth, but not for such large disparities as exist today." (Keynes, 1964, p. 374).

<sup>13</sup> Keynes also added a more subtle argument in defense of some degree of inequality, a point that was later developed by Hirschman (1977): "... dangerous human proclivities can be canalized into comparatively harmless channels by the existence of opportunities for money-making and private wealth, which, if they cannot be satisfied in this way, may find their outlet in cruelty, the reckless pursuit of personal power and authority, and other forms of self-aggrandisement. It is better that a man should tyrannise over his bank balance than over his fellow-citizens; and whilst the former is sometimes denounced as being but a means to the latter, sometimes at least it is an alternative. *But it is not necessary for the stimulation of these activities and the satisfaction of these proclivities that the game should be played for such high stakes as at present.*" (Keynes, 1964, p. 374, emphases added).

<sup>14</sup> One can speculate whether more philosophical, and less pragmatic, reasons could be involved in the acceptance by Keynes of some degree of inequality. A very compelling argument in favor of limited inequality was offered by one of his contemporaries, D.H. Lawrence: "Society means people living

concentration could increase beyond justifiable levels and become dysfunctional. Inheritances could be a source of dysfunctional concentration of income since individuals would enjoy riches without offering any compensation in return:

“I believe that the seeds of the intellectual decay of individualist capitalism are to be found in an institution which is not in the least characteristic of itself, but which it took over from the social system of feudalism which preceded it – namely, the hereditary principle. The hereditary principle in the transmission of wealth and the control of business is the reason why the leadership of the capitalist cause is weak and stupid.” (CWJMK 9, p. 299)

Moreover, the notion that consumption out of these riches could be considered as illegitimate to the point of threatening the political order had already been advanced in *The Economic Consequences of Peace*.<sup>15</sup>

Furthermore, the distributive problem could be attenuated by a sensible economic policy directed at keeping the economy at full employment, thereby generating higher rewards

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together. People *must* live together . And to live together, they must have some Standard, some *Material Standard*. This is where the Average comes in. And this is where Socialism and Modern Democracy come in. For Democracy and Socialism rest upon the Equality of Man, which is the Average. And this is sound enough, so long as the Average represents the real basic material needs of mankind: basic material needs: we insist and insist again. For Society, or Democracy, or any Political State or Community exists not for the sake of the individual, nor should ever exist for the sake of the individual, but simply to establish the Average, in order to make living together possible: that is, to make proper facilities for every man’s clothing, feeding, housing himself, working, sleeping, mating, playing, according to his necessity as a common unit, an average. Everything beyond that common necessity depends on himself alone.” Quoted in Williams (1983), p. 210, emphases and capital letters in the original.

<sup>15</sup> Cf. Keynes (1920), pp. 16ss. The view proposed here agrees with Schumpeter (1947), p. 80: “In those pages of the *Economic Consequences of the Peace* we find nothing of the theoretical apparatus of the *General Theory*. But we find that the whole of the vision of things social and economic of which that apparatus is the technical complement. The *General Theory* is the final result of a long struggle *to make that vision of our age analytically operative*.” (Schumpeter’s emphases)

for all society. Finally, since in his view excessive concentration was due to distorted institutions (such as the right to inheritance), its solution did not pose any special threat to the operation of the economy. Nothing of substance would be lost if the right of inheritance was altered.

The inability to generate or sustain full employment was a much more serious problem exactly because, in contrast with excessive income concentration, *it was caused* by the very same characteristic that went a long way in explaining why this type of economy is so efficient: its monetary character. Modern, advanced economies are organized on the basis of money contracts.<sup>16</sup> However, it is this very institution that turns money into a form of wealth, to be accumulated in competition to reproductive forms of wealth, such as, for instance, capital goods.<sup>17</sup> When one chooses to accumulate money, unemployment emerges.

Keynes's diagnosis was not one of hopelessness though. One could not solve the problem of unemployment merely by correcting existing institutions, although some reforms could be implemented to improve the situation, but one could do it through the enlightened implementation of economic policies. An active government could compensate the deficiencies of a capitalist economy if its goal was to sustain full employment.

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<sup>16</sup> "The introduction of a money, in terms of which loans and contracts with a time element can be expressed, is what really changes the economic status of a primitive society." (CWJMK 28, p. 255)

<sup>17</sup> "... there is always an alternative to the ownership of real capital-assets, namely the ownership of money and debts; so that the prospective yield with which the producers of new investment have to be content cannot fall below the standard set by the current rate of interest." (Keynes, 1964, pp. 212/213)

Enlightened government was Keynes's remedy to the shortcomings of capitalism. Not a totalitarian government, as in the case of the Soviet Union. Keynes defended a government focused on defending individual liberties, but a government anyway. Keynes didn't see this as a contradiction. As he wrote to Hayek commenting on the publication of the latter's *The Road to Serfdom*, a libel against government planning:

"I should say that what we want is not no planning, or even less planning, indeed I should say that we almost certainly want more. But the planning should take place in a community in which as many people as possible, both leaders and followers, wholly share your own moral position. Moderate planning will be safe if those carrying it out are rightly orientated in their own minds and hearts to the moral issue." (CWJMK 27, p. 387)

The keys to understand Keynes's views are: 1. to realize that he believed that governments could at last efficiently pursue the *common* good once conflict was demonstrated to be a thing of the past; *and* 2. the understanding that, once the problems were clearly defined and the right solutions identified, no one would be so irrational as to resist adopting the right policies. Keynes believed in the platonic idea of government of the sage but he also believed in rational persuasion. Armed with the right understanding of how the economy worked, an enlightened democratic government would implement the right policies.<sup>18</sup> As Keynes wrote, in defense of the creation of an

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<sup>18</sup> In a surprisingly warm assessment of Keynes's legacy originally published in 1989, Milton Friedman observed that "Keynes's bequest to technical economics was strongly positive. His bequest to politics, in my opinion, was not." (Friedman, 1997, p. 20). And the reason why he objected to Keynes's political views were the "two concepts implicit in his letter to Hayek: first, the public interest concept of government; second, the benevolent dictatorship concept that all will be well if only good men are in power." (idem). Friedman, like Hayek, was suspicious of government bureaucrats. In fact, he attributed Keynes's views to a double bias: on the one hand, Friedman argues that the British experience with the creation of a

Economic General Staff in the UK government:

“The foregoing may be open to the charge of magnifying unduly the functions and importance of what is proposed. But a move along these lines would indeed be an act of statesmanship, the importance of which cannot easily be exaggerated. For it would mark a transition in our conceptions of the functions and purposes of the state, and a first measure towards the deliberate and purposive guidance of the evolution of our economic life. It would be a recognition of the enormous part to be played in this by the scientific spirit as distinct from the sterility of the purely party attitude, which is never more out of place than in relation to complex matters of fact and interpretation involving technical difficulty. It would mean the beginning of ways of doing and thinking about political problems which are probably necessary for the efficient working of modern democracy. For it would be an essay in the art of combining representative institutions and the voice of public opinion with the utilization by Governments of the best technical advice in spheres, where such advice can never, and should not, have the last word or the poser, but

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professional body of highly competent civil servants working within a meritocratic system within an aristocratic political system favored the emergence of “a largely incorruptible civil service”. (id., p. 21). The other bias was generated by Keynes’s own biography: “Keynes’s own experience was also influential, particularly to economists. He set an example of a brilliant scholar who participated actively and effectively in the formulation of public policy – both through influencing public opinion and as a technical expert called on by the government for advice. He set an example also of a public-spirited and largely disinterested participant in the political process. And it is not irrelevant that he gained worldwide fame, and a private fortune, in the process.” (id., p. 22) Be it as it may, Friedman final verdict is severe: he argues that Keynes’s benevolent dictatorship would sooner or later degenerate into totalitarianism and that Keynes’s public success was due, to a large extent to the links between his economic theory and his political approach. In a sense, despite the warmth with which the paper was written, Friedman’s final view is the same as the one held by other conservative critics, that Keynes’s main (and unforgivable) fault was to legitimize the expansion of the power of the state.

must be a necessary ingredient in the decisions of those who have the power.” (CWJMK, 20, p. 27)<sup>19</sup>

However, as in his letter to Hayek, Keynes saw government action as a means to support a liberal society, not to supplant it. In his last published paper, Keynes quoted from a speech he delivered at the House of Lords to say:

“Here is an attempt to use what we have learnt from modern experience and modern analysis, not to defeat, but to implement the wisdom of Adam Smith.” (Keynes, 1946, p. 186)

These words were proffered with respect to the Bretton Woods agreement, but they somehow summarize Keynes’s views as to the role of policy-making and institution-building.

Keynes was indeed a radical critic of capitalism, but not in the now usual meaning of the word *radical*. In economic terms, the reach of his criticism was focused on the promotion of full employment macroeconomic policies and the adoption of reforms that could either eliminate excess income concentration and/or help to support full employment policies.

Keynes’s more general critique of capitalism was directed primarily at the fact that capitalism remained a type of social organization appropriate to situations of scarcity

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<sup>19</sup> The same feeling is concisely expressed in the statement: “I look forward with every emotion of satisfaction to the prospect that the world may be forced in my lifetime to the substitution of a scientific control of the lever which works the balancing factor in our economic life.” (CWJMK 20, pp. 164/165)

(even though Keynes argued that it was unable to maintain the full use of available resources). If the right policies allowed the capitalist social order to work its full potential, Keynes risked the estimate that a little more than a generation would be necessary to overcome scarcity.<sup>20</sup> In Keynes's terms, this meant that in this short space of time the expansion of investment would be enough to have the marginal efficiency of capital brought to zero.

Keynes's ultimate criticism of the capitalist order was aesthetic.<sup>21</sup> Capitalism made it impossible for humankind to dedicate itself to higher goals than earning their survival. But capitalism, led by enlightened government, could lead to its own obsolescence. Then humankind could finally dedicate itself to higher pleasures than just surviving or, even worse, money-making. To get an idea of Keynes's personal utopia, it is worth to quote at some extent from *The Economic Possibilities for Our Grandchildren*:

“Thus for the first time since his creation man will be faced with his real, his permanent problem – how to use his freedom from pressing economic cares, how to occupy the leisure, which science and compound interest will have won for him, to live wisely and agreeably and well. ... We shall be able to rid ourselves of many of the pseudo-moral

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<sup>20</sup> “On such assumptions I should guess that a properly run community equipped with modern technical resources, of which the population is not increasing rapidly, ought to be able to bring down the marginal efficiency of capital in equilibrium approximately to zero within a single generation ...” (Keynes, 1964, p. 220. A few years earlier, Keynes had been a little more circumspect: “I draw the conclusion that, assuming no important wars and no important increase in population, the *economic problem* may be solved, or be at least within sight of solution, within a hundred years.” (CWJMK 9, p. 326, emphasis in the original)

<sup>21</sup> Keynes's views at first sight could certainly be construed as an aristocratic critique of capitalism, the latter being viewed as a *rude* social order. But his approach was not the product of an idealization of a bucolic medieval past, as Raymond Williams has shown to be the case of many radical critics in England (Williams, 1983), in opposition to other radical critics that looked forward, beyond capitalism. In a curious manner, Keynes utopian future sounded like Marx's utopian future as outlined in *The German Ideology* (Cf. Marx and Engels, 1964). For an earlier critique of “reactionary socialism”, see Marx and Engels (1973), pp. 87/88.

principles which have hag-ridden us for two hundred years, by which we have exalted some of the most distasteful of human qualities into the position of the highest virtues. We shall be able to afford to dare to assess the money-motive at its true value. The love of money as a means to the enjoyment and realities of life – will be recognized for what it is, a somewhat disgusting morbidity, one of those semi-criminal, semi-pathological propensities which one hands over with a shudder to the specialists in mental disease. *All kinds of social customs and economic practices, affecting the distribution of wealth and of economic rewards and penalties, which we now maintain at all costs, however distasteful and unjust they may be in themselves, because they are tremendously useful in promoting the accumulation of capital, we shall then be free, at last, to discard.*” (CWJMK 9, pp. 328, 329, emphases added)<sup>22</sup>

### 3. Keynes and the Traditional Left

Keynes’s aversion to Marxism is well documented. He always referred to Marx’s *Das Kapital* in a especially harsh way, even though there is little evidence that Keynes has actually ever read it.<sup>23,24</sup> Even in those rare passages when a less hostile reference is made

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<sup>22</sup> Keynes utilizes the same moral angle to analyze communism: “Communism is not a reaction against the failure of the nineteenth century to organize optimal economic output. It is a reaction against its comparative success. It is a protest against the emptiness of economic welfare, an appeal to the ascetic in us all to other values.” (CWJMK 28, p. 35)

<sup>23</sup> In personal communication Professor Cristina Marcuzzo brought to my attention a letter from Keynes to Sraffa dated April 5, 1932, where Keynes wrote: “I made a good try at the Marx volumes, but I swear that it absolutely beats me what you find in them or what you expected me to find! I did not discover a single sentence of any conceivable interest to a rational human being. For next vacation you must give me a marked copy”.

to Marx, Keynes seems to be relying on secondary sources.<sup>25</sup> More representative of his views is the following statement:

“How can I accept a doctrine which sets up as its bible, above and beyond criticism, an obsolete economic textbook which I know to be not only scientifically erroneous but without interest or application for the modern world?” (CWJMK 9, p. 258)

The theoretical rejection was compounded by Keynes’s little appreciation for the Soviet experience. Reporting on his first visit to the country, in 1925, Keynes states that

“I sympathise with those who seek for something good in Soviet Russia. But when we come to the actual thing, what is one to say? For me, brought up in a free air undarkened by the horrors of religion, with nothing to be afraid of, Red Russia holds too much which is detestable.” (CWJMK 9, 258)

Keynes’s was repulsed by what he saw as the religious nature of Leninism.<sup>26</sup> Even Soviet political totalitarianism was explainable by its religious nature. Besides, he just could not make sense of what was the nature of the economic system proposed by the Bolsheviks.

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<sup>24</sup> There is also a remark in the famous letter to G.B. Shaw announcing the imminent publication of *The General Theory*, where Keynes states that after reading a volume with correspondence between Marx and Engels he had preferred Engels’ views. Cf. CWJMK 28, p. 42)

<sup>25</sup> The only non-hostile reference to Marx made by Keynes I could locate is also based on secondary sources, in this case the book by H.L. MacCracken. *Value Theory and Business Cycle*. Cf. CWJMK 29, p. 81.

<sup>26</sup> “Leninism is a combination of two things which Europeans have kept for some centuries in different compartments of the soul – religion and business. We are shocked because the religion is new, and contemptuous because the business, being subordinated to the religion instead of the other way round, is highly inefficient.” (CWJMK 9, p. 256)

In fact, Keynes's opposition to the Marxist left was multidimensional. First, as he made clear with notable candor, Keynes was openly an elitist:

“I can be influenced by what seems to me to be justice and good sense; but the *class* war will find me on the side of the educated *bourgeoisie*.” (CWJMK 9, p. 297, emphases in the original)

This, in fact, was one the (several) reasons he rejected Marxism:

“How can I adopt a creed which, preferring the mud to the fish, exalts the boorish proletariat above the bourgeois and the intelligentsia who, with whatever faults, are the quality in life and surely carry the seeds of all human advancement?” (CWJMK 9, p. 258)

Secondly, Keynes was a reformer, not a revolutionary, when choosing the *method* of change.<sup>27</sup> He wanted to preserve democratic parliamentary procedures and to use them to persuade the public of the desirability of his proposals. It seems that Keynes sincerely believed that established power and interests would not be capable of preventing an idea whose time had come from being accepted. When asked to explain why his ideas had not been more widely accepted if they were so good, Keynes replied:

“Dora Russel asks, ‘Why cannot we adopt a new economic policy drawn up by Mr Keynes to-morrow, if nobody is exerting power to prevent it?’ Because I have not yet succeeded in convincing either the expert or the ordinary man that I am right. If I am

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<sup>27</sup> “My own aim is economic reform by the methods of political liberalism.” (CWJMK 28, p. 29)

wrong, this will prove to have been fortunate. If, however, I am right, it is, I feel certain, only a matter of time before I convince both; and when both are convinced, economic policy will, with the usual time lag, follow suit.” (CWJMK 28, p. 35)

Thirdly, and perhaps more important, Keynes considered that despite their radical *political* opposition, laissez-faire ideas and Marxist ideas shared the same theoretical economic basis.<sup>28</sup>

Even though Keynes seemed to hold a soft spot for non-Marxist socialists, he opposed them not because they were radicals<sup>29</sup> but because, in his view, they had not understood the true nature of a capitalist economy and, therefore, pursued the wrong goals. For Keynes, Marxism shared the Ricardian legacy with laissez-faire capitalism. Both had analyzed the workings of a non-monetary economy. Keynes’s criticism of the policy implications of classical theory, in the first chapter of *The General Theory*, would equally apply to Marxist proposals to overcome capitalism. Keynes believed that understanding the nature of monetary economies would lead to different policy proposals, not only in terms of managing capitalism but also of transforming and, ultimately, overcoming it.

The key to understand Keynes’s reform program is to see that income and wealth redistribution is not only a question of legitimacy and social justice, it is also a question of *efficiency*. Taxing large incomes and wealth prevented conspicuous consumption that

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<sup>28</sup> Cf. CWJMK 28, pp. 31/32.

<sup>29</sup> Keynes observed that in some aspects he considered himself to be at the left of the Labor Party, for example. Cf. CWJMK 21, pp. 372/373.

would subtract from the legitimacy of capitalism.<sup>30</sup> Reducing conspicuous consumption should not imply reduction of consumption per se. That is where redistribution would be fair *and* efficient. Sustaining full employment was a task for macroeconomic policy, but the latter would work much better with a stronger propensity to consume and, as a result, a high multiplier. Besides, larger consumption expenditure would also create new investment opportunities, supporting aggregate demand in the short term and accelerating capital accumulation in the long. Social reform would thus facilitate sustaining full employment in the short term, and, in the long, full employment would facilitate social reform .

Redistributive schemes favored by Keynes also played a complementary role of regularizing the business cycle. The ideal moment for implementing income redistribution initiatives would be when the economy was beginning a recession so that distribution would boost aggregate demand maintaining the economy, as Keynes wrote in *The General Theory*, in a *quasi-boom*.

These reforms should be enough to remove what Keynes saw as the shortcomings of the system while preserving its virtues. Among these virtues Keynes counted the freedom of individuals to decide what to do with their income. Even though he cautioned about pervasive market imperfections that made actual capitalism very different from what was

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<sup>30</sup> The prominence of proposals to reduce taxes or to diminish their degree of progressiveness in current conservative political platforms reminds us how politically charged this subject is. Keynes's arguments in favor of progressive taxes and against the right to inheritance could be construed as very radical views. In fact, in the ten-point program offered by Marx and Engels in the 1848 Communist Manifesto, the second point was precisely "a heavy progressive or graduated income tax". The third proposal was "abolition of all right of inheritance". Cf. Marx and Engels (1973), p. 86.

idealized by laissez-faire ideologues, Keynes still seemed to believe that the evolution of joint-stock companies had already been a large step in the direction of a more balanced economic system. Developing and perfecting this type of organization seemed to him more promising than either the individualistic capitalism of the nineteenth century or the state control as practiced in the soviet economy.

#### *4. Two Reform Proposals (I): How to Pay for the War<sup>31</sup>*

As we saw, ideal social reforms would be those combining income redistribution, sustaining aggregate demand and regularization of the business cycle. The war years would allow Keynes to advance, or to participate in, the debate of two such proposals. The first began with a debate around the methods to finance the war effort.

Financing the war effort required, in fact, solutions to two different problems. The first was a public finance question: the government had to raise enough money to pay for the expenses of supporting an army, supplying weapons and ammunitions, etc. There were three financing alternatives at the reach of government: raising taxes, borrowing or issuing money thereby collecting *seigniorage* and the inflation tax. The second problem was macroeconomic: how to generate real resources to be used up in the war effort. These were more or less normal problems in the operation of an entrepreneurial economy, but they were now magnified by the context of total war.

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<sup>31</sup> This section is based on Carvalho (2006).

Traditionally, inflation had played a central role in solving both the public finance and the macroeconomic problems. Inflation reduces workers' consumption and allows government to raise revenues by taxing extra-profits. *How to Pay for the War* was born of Keynes's concern with the wastefulness and unfairness of this financing method. Besides, inflation increased domestic social tensions and these tensions were likely to reach unacceptable levels given the demands of total war.

The plan proposed by Keynes in February 1940 was relatively simple. Whatever real resources were necessary to pursue the war would be appropriated by the government one way or another, so they would not be available to satisfy private consumption demands (which would rise, given the increase in employment caused by increased aggregate demand). The transfer of goods to the government could take place via increased taxes or through inflation. In both alternatives, the workers' increased incomes would be actually confiscated by the government without any compensation for the increased efforts of labor. Keynes offered a different plan: instead of confiscating labor incomes, the value of the income surplus over affordable consumption would be deposited in interest-earning personal accounts to be returned to the workers after the war. Both the traditional methods and the new one proposed by Keynes implied that workers would not be able to increase their consumption. The essential difference between them resided in the fact that Keynes's plan would work as a forced savings scheme leading to increased wealth to workers after the war while in the traditional method "the working class did their extra work for nothing." (CWJMK 22, p. 78)

The scheme consisted in four measures. The first was the creation of a compulsory savings fund in which a variable proportion of each worker's income would be deposited for the duration of the war (CWJMK 9, p. 379). Accumulated savings plus interest would thus constitute workers' capital. The second measure was to raise the funds to redeem this debt through the imposition of a capital levy (CWJMK 9, p. 379). Compulsory savings were not to be destined to investments but to finance the war effort. Thus, the resources necessary to redeem the debt could not be generated by the fund itself being necessary to define alternative sources of funds. Keynes chose a capital levy attending a suggestion of Hayek.<sup>32</sup> The third measure established some exemptions, as in the cases of workers' earning incomes below a given minimum. The fourth measure was to index the value of the compulsory savings to wage-goods prices so as to preserve its real purchasing power.

The deferred pay plan (as Keynes decided to name it, considering that the expression "deferred pay" would be simpler to grasp) became thus a wealth redistribution plan.

The deferred pay plan would also contribute to fight unemployment and regularize the business cycle. Redemption would be scheduled to happen at the onset of the first post-war recession, contributing therefore to boost consumption demand when it began to sag. Income (and wealth) redistribution and fighting unemployment: the plan would contribute to reduce the two evils of capitalism.

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<sup>32</sup> CWJMK 22, p. 92n.

Keynes didn't waste too much time to realize that the deferred pay plan, in fact, could be generalized to deal with every situation of excess demand. In his words:

“I am not proposing an expedient, undesirable for its own sake, just for the purpose of financing the war. I am seizing an opportunity, where the need is obvious and overwhelming, to introduce a principle of policy which may come to be thought of as marking the line of division between the totalitarian and the free economy. For if the community's aggregate rate of spending can be regulated, the way in which personal incomes are spent and the means by which demand is satisfied can be safely left free and individual.” (CWJMK 22, p. 123)<sup>33</sup>

Facing opposition from the Labor Party, that preferred a scheme where the war effort was entirely financed by taxes on profits, which Keynes considered far from enough, he argued in an even more pointed way:

“With these additions, it seems to me that it would be extraordinarily misguided of Labour to refuse the arrangement, which is not merely a piece of technique to solve the war problem, *but is taking advantage of war conditions to introduce important new social reforms and to make a much greater move towards equality than has been made for a long time past.*” (CWJMK 28, p. 138, emphases added)

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<sup>33</sup> “... there are, I think, important social advantages in accumulating deferred pay to increase working class resources and consumption after the war, thus rewarding present effort when once again we have a surplus capacity. It will have the positive advantage when the time comes of preventing unemployment. Meanwhile it will provide the working classes with better security against misfortunes and with increased wealth; - for a right to deferred consumption is precisely what wealth is.” (CWJMK 22, pp. 95/96)

### 5. Two Reform Proposals (II): The Beveridge Plan<sup>34</sup>

The Beveridge Plan was presented in the document *Social Insurance and Allied Services*<sup>35</sup>, containing specific proposals to extend and improve the then-existing social security system in England. In the report “the term ‘social security’ is used ... to denote the securing of an income to take the place of earnings when they are interrupted by unemployment, sickness or accident, to provide for retirement through age, to provide against loss of support by the death of another person, and to meet exceptional expenditures, such as those connected with birth, death and marriage.” (§ 300).

Social security was conceived to guarantee a minimum subsistence income to all the population, seeking to abolish “want” (§ 11). It would include, as mentioned above, payments for many contingencies, and it would be funded by contributions of employees, employers and the State. Its “socialistic” nature was rooted in the severance of the link between income and services performed.

The scheme relied on three assumptions: “(A) children’s allowances for children up to the age of 15 or if in full-time education up to the age of 16; (B) comprehensive health and rehabilitation services for prevention and cure of disease and restoration of capacity to work, available to all members of the community; (C) Maintenance of employment, that is to say avoidance of mass unemployment.” (§ 301).

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<sup>34</sup> For a larger view of the relationship between Keynes and Beveridge in ways that parallel the one followed in this paper see Marcuzzo (2006).

<sup>35</sup> This was a report presented by Sir William Beveridge to Parliament by Command of His Majesty, in November 1942. The report run more than 300 pages, but a kind of executive summary extracted from the report itself can be found at [www.fordham.edu/HALSALL/MOD/1942beveridge.html](http://www.fordham.edu/HALSALL/MOD/1942beveridge.html).

The last assumption is in fact a key feature of the Plan. Social security was not an alternative to full employment policies. It would set a floor under aggregate demand through the maintenance of a minimum income level to consumers even in the presence of unemployment, but it could work as such only if unemployment was kept under control by the government. “The Government should not feel that by paying doles it can avoid the major responsibility of seeing that unemployment and disease are reduced to the minimum.” (§ 22)

The Beveridge Plan for social security was in strict accord with Keynesian reformism. It promoted income distribution through the protection against earnings losses, universal provision of health services and children’s allowances. It worked to put a floor under aggregate demand so demand would not fall as much as employment in recessions, contributing to reduce output volatility. Finally, while the social insurance elements (retirement provisions) were to be funded by employees, employers and the State, the social assistance elements would be funded by the State.

Keynes reacted to the report in a letter to Beveridge. In the letter Keynes wrote:

“... let me say that I have read your Memoranda, which leave me in a state of wild enthusiasm for your general scheme. I think it a vast constructive reform of real importance and am relieved to find that it is so financially possible.” (CWJMK, 27, 204)

In the following years, Keynes played an active role in the development of the scheme, helping to ensure its financial viability, discussing entitlements, contributions, and access conditions. Keynes raised some minor objections to specific clauses and was able to persuade Beveridge to change some of them. Keynes's efforts were necessary because of the skepticism of some Treasury members as to the feasibility of the proposal. The importance Keynes gave to the Plan is witnessed by his intention to dedicate his maiden speech in the House of Lords to its defense. In the draft speech, that in end was not delivered, Keynes dares the country to rise up to the challenge of promoting such a reform program. His words could not be more eloquent:

“My Lords, a refusal, if it had been made, to commit later years to this modest extent would have raised the whole question of our attitude to the future. The future will be what we choose to make it. If we approach it with cringing and timidity, we shall get what we deserve. If we march on with confidence and vigour the facts will respond. It would be a monstrous thing to reserve all our courage and power of will for War and them, crowned with victory, to approach the Peace as a bankrupt bunch of defeatists.”  
(CWJMK 27, 260)

To those who feared that the Plan would be too expensive, Keynes offered once more his vision of the future:

“Looking beyond the immediate post-war period, when our economic difficulties will be genuine and must take precedence over all else – perhaps for the last time – the economic

problems of the day [that] perplex us, will lie in solving the problems of an era of material abundance not those of an era of poverty. It is not the fear of a failure of physical productivity to provide an adequate material standard of life that fills me with foreboding. The real problems of the future are first of all the maintenance of peace, of international co-operation and amity, and beyond that the profound moral and social problems of how to organize material abundance to yield up the fruits of a good life. These are the heroic tasks of the future.” (CWJMK 27, 261)

## 6. Conclusion

The deferred pay plan and the Beveridge plan had at least two common characteristics: they were intended to promote income (and, in the case of the deferred pay plan, also wealth) redistribution and to contribute to regularize aggregate demand through the definition of a floor to aggregate demand. Thus, both represented direct attacks on the two evils of the capitalist system identified by Keynes in *The General Theory*. It should not thus be surprising the enthusiasm with which Keynes conducted the debate around the deferred pay scheme and participated in the defense of the social security plan.

The reforms were socialist in at least two senses. Firstly, they would at least partially break the linkage between income earning and market performance, severing the ties between supply and demand of productive factors and income access. Secondly, the State would assume direct responsibility for promoting income re-distribution. On the other hand, there is also a conservative streak in the reforms. They would help to restore the

legitimacy of the social order by attenuating class differences and eliminating extreme privileges. Moreover, they would not require any changes in the organization of production as such or in the roles of the consumer and the producing firm in the allocation of resources.

It has been observed by many authors that Keynes did not object to the intervention on the productive process in principle. In fact, in the 1920s Keynes explored many possibilities of reorganization of the productive system, mostly based on the idea that joint-stock companies were already closer to a public company model than to the individualistic capitalism of the nineteenth century.<sup>36</sup>

The incrementalist nature of the two reforms also agreed with Keynes's disposition against revolutionary political changes. Keynes's political views, however, remain a difficult subject given his very peculiar brand of Platonism, whereby elites should decide on policies while, at the same time, the political system would remain democratic since there would be no basis for conflict once policy-making became informed by Keynesian theories.

Be it as it may, when the distributive emphasis of social reforms proposed or supported by Keynes are made clear, one can realize that the proximity of his views with the

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<sup>36</sup> Most of these discussions are collected in CWJMK, 19. Among recent explorations of these and other writings by Keynes, see Crotty (1999). It is interesting to realize that many of these ideas Keynes developed previously to the publication of *The General Theory* were in fact incorporated in social democrat political programs, particularly in Scandinavian countries. Scandinavian social democracy is Keynesian because of its acceptance of Keynes's views as to how to promote structural change in the productive sector rather than because of Keynesian macroeconomic policies. Compare, for instance, the writings mentioned in the beginning of this footnote with Glyn (1998), Vartiainen (1998) and Iversen (1998).

Scandinavian social democracy, with Western democratic socialism or with US liberalism as practiced by FDR and, later, by Lyndon Johnson, is more effective than what is usually acknowledged. Neither of these reformist movements relied on deficit spending, that many analysts still think to be the essence of Keynes's revolution. All of them, on the other hand, took steps to promote income redistribution and, in the process, strengthened the institutions supporting full employment. In this sense, there is no question as to whether or not Keynes belonged to the left tradition.

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