Is A Steady-State Economy Compatible With Capitalism?

There are several reasons why capitalist economies are *compelled* to grow – why, as James Gustave Speth put it, "the capitalist economy, to the degree it is successful, is *inherently* an exponential growth economy."[1] All those reasons revolve around the nature of profit…

Profits

Competition for profits compels growth because businesses that gain profits are obliged to invest much or all of them in new ventures intended to *increase* their profits, thus boosting production and spending, which means economic growth. If businesses don't reinvest, they risk shrinking profits and ultimate loss, because either their markets will become 'saturated' with too many consumers already having purchased their goods, or newer products will supersede theirs, or they will be out-competed by other businesses that do grow.

Jobs

But not only businesses have compelling reasons to want economies to grow, so do wage earners. If an economy does not grow, if instead its spending reduces, it has less need for production and work – and because less work almost invariably means less income, this causes obvious problems, not only for those whose income reduces, but also for producers of the goods that might otherwise have sold if income had not reduced. Failure to grow thus encourages more of the same. Or as Tim Jackson put it: "Growth is *necessary* within this system just to prevent collapse."[2]

Debt

As well as businesses and workers, banks and other financial institutions have a vested interest in the creation of jobs and maintenance of growth: for loans to producers to be repaid, they must finance enterprises that eventually make sufficient profits to cover the costs of servicing the loans, which means more spending. Similarly, if consumers spend less, not only do they have less need to borrow money, but also fewer sales happen, and therefore profits reduce, leaving businesses with less money to repay debts. So, like any profit-seeking business, lenders want growth.

Compelled to Grow

So, any economy which involves market competition for profits is *compelled* to grow. But because capitalism is more or less defined by market competition for profits, this means that *the compulsion to grow is built into capitalism's game rules.*

Now if a capitalist economy must grow, whereas a steady-state economy, by definition, does not grow, then a capitalist steady-state is an oxymoron.

An Unsteady State

Jackson claimed that "The capitalist model has no easy route to a steady-state position. Its natural dynamics push it towards one of two states: expansion or collapse."[3] I would agree with this completely if the word "easy" had been left out.

Consider what would happen if a capitalist economy's spending somehow did stay static for an extended period, neither growing nor contracting: efforts to gain profits would still eventually unleash productivity improvements that reduce the need for workers, meaning less money distributed as wages to afford the same amount of output (or more) – but this would mean *less* spending ie. contraction, which, as explained, threatens collapse for a capitalist economy. Borrowing could compensate for reduced wages, but only temporarily, because paying back a loan with interest requires saving more than what the loan allows to be spent – so, the eventual effect would still be less spending. *Mounting*

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[1] James Gustave Speth, *The Bridge at the End of the World: Capitalism, the Environment, and Crossing from Crisis to Sustainability* (Yale University Press, New Haven & London, 2008), p.59 (my italic)

[2] Tim Jackson, *Prosperity without Growth? The Transition To A Sustainable Economy* (Sustainable Development Commission, 2009, available at http://www.sd-commission.org.uk/publications/downloads/prosperity_without_growth_report.pdf), p.8 (my italic)

[3] Jackson, *Prosperity Without Growth*, p.46

debt might maintain a steady-state, but sustaining an appropriate rate of increase of debt is not an easy task; more fundamentally, a steady-state with mounting debt is a contradiction in terms.

So, to avoid collapse, a capitalist steady-state would require some other approach to compensate for the effects of productivity improvements. One such approach has been proposed…

A Model Future?

An economic model by Peter Victor (cited by Jackson[4] and a recent Steady State Economy Conference (SSEC) report[5]) gains a roughly steady-state after 25 years, by shifting "investment from private to public goods", redistributing income to reduce inequality, sharing work, and lowering working hours as productivity increases (as it is assumed to do[6]). These seem worthwhile goals, but hardly natural outcomes of market competition (even with the role of government clearly expanded to make for a more regulated economy than today's). Even so, after 25 years the modeled steady-state still retains sixty percent of initial unemployment, half the initial poverty levels (for the last 15 or more of its 25 years), and slowly mounting government debt, all of which strike me as inadequate outcomes.

More crucially, while Victor's model is tailored to achieve no growth, it does so without including "a monetary sector",[7] and without addressing the consequences for business profits: with higher productivity still leading to less income (albeit more evenly shared) to afford the same output, spending must *reduce*, which, along with less business investment, must decrease profits – an outcome directly opposed to standard business goals, and, as previously explained, encouraging collapse, *not* a steady-state.

Jackson rightly suggests that the model's results should be viewed "with caution",[8] and the SSEC report advises similarly, but the failure to include profits in the model[9] puts its results in doubt. Furthermore, the model, like the SSEC report, has not considered a crucial but generally overlooked profit-driven dynamic of competitive market economies…

The Profit Paradox

Although the subject has been largely ignored since the Great Depression, luminaries such as Marx and Keynes long struggled to explain the 'profit paradox': money distributed during production of goods – the payments made to do the producing – sums to less than the money required to buy those goods, because prices include a profit margin, an amount over and above the cost of the goods. So how can producers profit in aggregate? In my view, and those of some economists,[10] they can't: if any competitor profits, another must lose.

Loss can be delayed by consumers taking on debt to afford profit-inclusive prices of producers otherwise doomed to lose because others profit – but repaying consumer debt requires *eventually* foregoing some other purchase, which again means that eventually not every producer profits, or else the consumer defaults on the debt and the lender fails to profit. In the long run then, overall, taking producers' *and* lenders' profits and losses into account, aggregate profits still must be zero.

The only way for profits to consistently exceed losses is via *mounting* consumer debt, but as mentioned, not only is this incompatible with a steady-state, it is also unsustainable – even in a growth economy, as demonstrated by the credit crisis that unleashed the Great Recession. Ultimately, even mounting debt does not solve the profit paradox.

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[4] Jackson, *Prosperity Without Growth*, pp.79-81

[5] O'Neill, D.W., Dietz, R., Jones, N. (Editors), 2010. *Enough is Enough: Ideas for a sustainable economy in a world of finite resources. The report of the Steady State Economy Conference*. Center for the Advancement of the Steady State Economy and Economic Justice for All, Leeds, UK, p.37

[6] Jackson, *Prosperity Without Growth*, p.80

[7] Jackson, *Prosperity Without Growth*, note 28, p.81

[8] Jackson, *Prosperity Without Growth*, note 28, p.81

[9] Victor, P. and Rosenbluth, G. 2007. Managing without growth. *Ecological Economics* 61:492-504 (available at http://steadystate.org/wp-content/uploads/Victor_ManagingWithoutGrowth_EE_Paper.pdf) explains that the model includes a "corporation profits tax" rate, but makes no other reference to profits.

[10] Many 'Circuitist' economists. Also, see Gunnar Tomasson & Dirk J. Bezemer, "What is the Source of Profit and Interest? A Classical Conundrum Reconsidered" (University Library of Munich MPRA Paper #20320, 2010, available at http://ideas.repec.org/p/pra/mprapa/20320.html).

So, because profits make losses inevitable – and losses encourage unemployment, bankruptcy and reduced spending – whether a profit-based economy aspires to growth *or* a steady-state, instability is guaranteed. Profit-inclusive prices also fail to ensure efficient use of resources: even ignoring how prices function so poorly as market signals (because, among other reasons, they exclude externalities and government subsidies, but include market waste and excess), an efficient producer can still lose if another equally efficient producer wins. Although efficiency undoubtedly plays a role, the nature of profit ensures that so too does chance.

Flawed Motive

A steady-state and profit are diametrically opposed: the former aims for balance, the latter for gain – for obtaining something *extra*. Indeed, with capitalism, just as for a Ponzi scheme, the aim is to get more money back than is put in – not just for businesses via profit and banks via interest, but also for investors via their invested money. But just as Ponzi schemes eventually unravel, so too must capitalist expectations be disappointed: to have more returned than is contributed overall cannot be maintained, indeed, ultimately makes no sense.

Biting the Bullet

Capitalism and a steady-state economy are not compatible, either philosophically or practically. Although necessary for true sustainability, a steady-state economy cannot be achieved if businesses compete for profits. A steady-state economy requires the abolition of both profit (and interest) – indeed, it requires a *new* 'ism'.

Herman Royce is God Almighty's biographer and self-appointed spokesperson, inventor of A Free Lunch, and the first person in history to say "Now I've seen you naked, I could never eat turkey."