

Unit 13

Evolution, Development and Function of Capitalism

Contents

- 13.1 Introduction
- 13.2 Historical Interpretations of Capitalism
- 13.3 Development and Function of Capitalism
- 13.4 Commodity Production and Capitalist Production
- 13.5 Expansion of Markets and Production
- 13.6 Monopoly Capitalism and Imperialism
- 13.7 Conclusion
- 13.8 Further Reading

Learning Objectives

This unit is aimed at contributing towards an understanding of

- the evolution, development and function of Capitalism
- also provide different theoretical standpoints on Capitalism through historical writings

13.1 Introduction

Capitalism was used by economists in a purely technical sense to refer to the use of methods of production, and has been largely associated with a particular view of the nature of capital. This definition of capitalism has no reference to the way in which the instruments of production are owned. It refers only to their economic origin and the extent of their use. According to another conception, capitalism is identified with a system of unfettered individual enterprise. That is a system where economic and social relations are ruled by contract, where men are free agents in seeking their livelihood, and where legal compulsions and restrictions are absent. Thereby capitalism is made virtually synonymous with a regime of *laissez-faire* or free competition.

13.2 Historical Interpretations of Capitalism

Broadly speaking, historical research and historical interpretation have influenced three separate meanings assigned to the notion of capitalism.

a) Capitalism as a Spirit of Enterprise

This idea has been popularised by the writings of Werner Sombart. He has sought the essence of capitalism, not in any one aspect of its economic anatomy or its physiology. But in the totality of those aspects as represented in the *geist* or spirit that inspired the life of a whole epoch. This spirit is a synthesis of the spirit of enterprise or adventure with “bourgeois spirit” of calculation and rationality. Believing that at different times different economic attitudes have always reigned, and that it is this spirit which has created the suitable form for itself and thereby an economic organisation. Thus he traced the origin of capitalism in the development of states of mind. And hence, human behaviour is conducive to the existence of those economic forms and relationships which are characteristic of the modern world.

The pre-capitalist man was "a natural man" who conceived economic activity as simply catering to his natural wants. And in pre-capitalist times "at the centre of all effort and all care, stood living man": he is the measure of all things. By contrast, the capitalist, turned topsy-turvy the natural man - his primitive and original outlook and all the values of life, and saw the amassing of capital as the dominant motive of economic activity. And in an attitude of sober rationality and by the methods of precise quantitative calculation, subordinated everything in life to this end.

More simply, Max Weber defined capitalism as "present wherever the industrial provision for the needs of a human group is carried out by the method of enterprise". Weber used the spirit of capitalism to describe that attitude which seeks profit rationally and systematically".

b) Capitalism as a Commercial System

This is the meaning more often found implicit in the treatment of historical material than explicitly formulated. This notion virtually identifies capitalism with the organisation of production for a distant market. However, the regime of the early craft guild, where the craftsman sold his products retail in the town market, would presumably be excluded by this definition. Capitalism could be regarded as being present as soon as the acts of production and retail sale came to be separated in space and time by the intervention of a wholesale merchant. This merchant advanced money for the purchase of wares with the object of subsequent sale at a profit. To a large extent this notion is a lineal descendent of the scheme of development employed by the German Historical School, with its primary distinction between the "natural economy" of the medieval world and the "money economy" that succeeded it. Money economy emphasized that the 'market' defined the stages in the growth of the modern economic world.

In the words of Bucher, the essential criterion is "the relation which exist between the production and consumption of goods. To be more precise, the length of the route which the goods traverse in passing from producers to consumers. This is not uncommonly found in close conjunction with a definition of capitalism as a system of economic activity that is dominated by a certain type of motive or profit motive. The existence in any period of a substantial number of persons who rely on the investment of money with the object of deriving an income, whether this investment be in trade or in usury in production being taken as evidence of the existence of an element of capitalism. Prof. Naussbaum defines Capitalism as "a system of exchange economy" in which the orienting principle of economic activity is unrestricted profit. To which he adds an additional characteristic, saying such a system is marked by a differentiation of the population into "owners and property-less workers".

c) Capitalism as a Particular Mode of Production

We have the meaning originally given by Marx, who sought the essence of capitalism neither in a spirit of enterprise nor in the use of money to finance a series of exchange transactions with the object of gain, but in a particular mode of production. By mode of production, he did not refer merely to the state of technique, what he termed as the state of productive forces. But to the way in which the means of production were owned and to the social relations between men which resulted from their connections with the process of production. Thus capitalism was not simply a system of

production for the market — but a system of commodity of production as Marx termed it. And also it is a system under which labour-power had “itself become a commodity” and was bought and sold on the market like any other object of exchange.

The historical prerequisite of capitalism was the concentration of ownership of the means of production in the hands of a class, consisting of only a minor section of society. As a consequence of this, a large-scale property-less class emerges, for whom the sale of their labour power was their only source of livelihood. Accordingly, productive activity was accomplished by the property-less class not by virtue of legal compulsion, but on the basis of a wage-contract. It is clear that such a definition excludes the system of independent handicraft production where the craftsman owned his own petty implements of production and undertook the sale of his own wares. However, here there was no divorce between the ownership and work; and except where he relied to any extent on the employment of journeymen, it was the purchase and sale of inanimate wares not of human labour-power that was his primary concern.

What differentiates the use of this definition from others is that the existence of trade and of money lending and the presence of a specialised class of merchants or financiers. Even though they may be men of substance, it does not suffice to constitute a capitalist society. Men of capital, however acquisitive are not enough; their capital must be used to yoke labour to the creation of surplus value in production.

d) Reflections on the origin of capitalism

Both Sombart’s conception of the capitalist spirit and a conception of capitalism as primarily a commercial system share in common certain lacunae.

- These conceptions focus acquisitive investment of money.
- These conceptions are insufficiently restrictive to confine the term to any one epoch of history.
- And that they seem to lead inexorably to the conclusion that nearly all periods of history have been capitalist, at least in some degree.

The further difficulty attaches to the idealist conception of Sombart and Weber and their school, that if capitalism as an economic form is the creation of the capitalist spirit, the genesis of the latter must first of all be accounted for before the origin of capitalism can be explained. If this capitalist spirit is itself an historical product, what caused its appearance on the historical stage? To this riddle, no satisfactory answer has been propounded to date, other than the accidental coincidence in time of various states of mind.

Box 13.1: Protestantism and Capitalism

The search for a cause has led to the unsatisfactory and inconclusive debate as to whether it is true that Protestantism gave rise to the capitalist spirit (as Weber and Troeltsch have claimed). There seems to be scarcely more reason to regard capitalism as the child of the reformation than to hold, with Sombart that it was largely the creation of the Jews. However, if the emergence of a new economic system is to be explained in terms of an idea, this idea must embody in its “embryo” the essence of the future system in advance, which has to be explained. On the other hand, the definition of capitalism in actual use in historiography has moved increasingly towards that which was first adopted and developed by Marx.

Emphasis has increasingly come to be placed on the emergence of a new type of class differentiation between capitalist and proletariat rather than on profit as a motive of economic activity. And attention has increasingly been focussed upon the appearance of a relationship between producer and capitalist, analogous to the employment relation between master and wage earner in the fully mature industrial system of the 19th C. On the whole, this is because the material which research has disclosed, has forced this emphasis upon the attention of historians in their search for the essential differentiation of the modern age, than because they have been predisposed towards it by the writings of Marx. Thus Mr Lipson in claiming that the essentials of capitalism were present some centuries before the industrial revolution, states that "the fundamental feature of capitalism is the wage-system under which the worker has no right of ownership in the wares which he manufactures. The worker sells not the fruits of his labour but the labour itself, a distinction which, is of vital economic significance.

13.3 Development and Function of Capitalism

a) Stages of Capitalism

The development of capitalism falls into a number of stages characterised by different levels of maturity. Each of them is recognizable by fairly distinctive traits only when we seek to trace the stages and to select one of them as marking the opening stage of capitalism. If we are speaking Capitalism as a specific mode of production, then it follows that we cannot date the dawn of this system from the first signs of the appearance of large-scale trading and of a merchant class, and we can not speak of a special period of merchant capitalism. We must look for the opening of the capitalist period only when changes in the mode of production occur, in the sense of a direct subordination of the producer to a capitalist. This is not just a point of terminology, but of substance.

The Main work of Marx carries the title: "Capital". Marx spent many years of his life on the analysis of capitalism, because he was convinced that a thorough theoretical understanding was needed in order to facilitate the practical critique of capitalism, its overthrow by the proletariat. As the subtitle puts it, "Capital" is "A Critique of Political Economy". Political Economy stands for the economic theory developed by the classical bourgeois economists like Adam Smith and David Ricardo. Marx studied their theories in minute detail. Starting their theories and subjecting their categories such as value, commodity, money, capital, etc, to a sharp critical analysis, Marx proceeds to expose the true nature of capitalism. In the process he breaks down the powerful scientific legitimation of capitalist economy and not only provides a new scientific model for the analysis of capital, but lays the foundations for a fundamental critique of the totality of capitalism.

b) Political Economy of Capitalism

There are two ways to study capitalism and to get to know its specific character and both ways we need in order to get a full understanding. The first way is to study its history, how it was born, how it developed, under which circumstances, and with what results. This requires a study not only of the economic process but of the development of the whole bourgeois society. It is wide field, as each country has its own history in this respect. But such studies presuppose the second way to study capitalism, namely the systematic analysis of the economic structure of capitalist society. In that

case one has to start not from the historical origins, but from the capitalist system as a totality. That is the approach, which Marx follows in "Capital".

Box 13.2: Dialectical Logic

Historically one would have to begin with agriculture and the category of ground-rent. By taking capital as starting point and finishing point Marx follows the path of dialectical logic. This method presupposes the concrete totality of the system, but for the sake of analysis it takes one part after the other till it is able to conceive and present how all aspects, all relations, all categories, function as parts of totality. Marx calls it the method of rising from the abstract to the concrete. The isolated part may look real and concrete, but it is an abstraction from the more complex reality. It is the "rich totality of many determinations and relations" which forms the concrete reality.

Capital is constructed according to this dialectical logic. Volume I is devoted to the analysis of "The process of production of capital". We can neither discuss all the theories forwarded by Marx in "Capital" nor can we go into the specifics of the historical development of capitalism. We can only highlight some of the main theoretical statements and refer to some of the main aspects of the historical process.

13.4 Commodity Production and Capitalist Production

A first characteristic of capitalist economy is that it is a form of commodity production i.e. production for sale, production for the market. That is why Marx starts his analysis of the capitalist mode of production with the analysis of "commodities". But not all commodity production is already capitalist production. Commodity production emerged thousands of years back in human history whereas capitalism is only a few hundred years old. In primitive society all production is for direct use, there is no production for exchange on the market. Production of commodities, of goods for exchange, developed slowly. For a long time, it plays only a subordinate role. Only in capitalist society commodity production becomes the completely dominant form of production, it becomes generalised.

Reflection and Action 13.1

Is commodity production a recent phenomenon? Give some of its characteristics.

Analysing the mode of simple commodity production, Marx characterises the purpose as : to sell in order to buy. The peasant wants to sell some grain in order to buy grain. The weaver comes to sell some cloth in order to buy grain. The operation can be presented as C-M-C. i.e. Commodity - Money - Commodity. One sells one commodity in order to buy another commodity. Money is a means of exchange, just to make the transaction easier. The value of the two commodities, of C and C, is the same, is equivalent. However, on the market place we find not only the peasant and the artisan, but also the merchant. His economic operation is a different one: he buys in order to sell. He comes to the market not with commodities but with money. With that money he buys some product in order to sell it a higher price. This operation can be presented as M-C-M i.e. Money-Commodity-Money with increased value. This money which has been increased by a

surplus-value is called capital. Capital has been there long before capitalism, in the form of merchant capital or usurer-capital, money-lender capital. The difference is that these forms of capital derive their profit from their role in the exchange of commodities, in the sphere of distribution, of circulation, of the market. The usurer and the merchant appropriate part of the surplus-value which has been produced, but they don't control the production itself.

The capitalist mode of production comes into being when capital moves into the sphere of production, when it gets hold of the means of production and starts controlling and directing production itself. This is a long historical process, which starts in Medieval Europe. Its basic characteristics are:

- The separation of the producer from his means of production;
- The concentration of the means of production in the hands of one class, the bourgeoisie;
- The formation of another class, which has no means of subsistence other than the sale of its labour power, the proletariat.

Capitalist production is impossible as long as the producers still own or control the means of production. As long as an artisan, a weaver or a carpenter, has his own tools and workshop, he will not voluntarily go and sell his labour-power and start working in a factory. As long as a peasant possesses some land he will prefer to work on it rather than get hired as a labourer. Capitalist production needs workers, people who sell their labour-power. Therefore, it needs the separation of producers and means of production, so that the producers are forced by economic compulsion to sell their labour-power.

This separation has taken place in various ways, usually in a very brutal and bloody manner. "In actual history, it is notorious that conquest, enslavement, robbery, murder, briefly force, played the greater part". Marx has documented this for England in capital I, part VIII, ch.26., showing that the "so-called primitive accumulation" is "nothing else than the historical process of divorcing the producer from the means of production".

The result of this process of separation is the formation of two classes, which form the two poles of capitalist society. On the one side we find the bourgeoisie as the class of owners in whose hand the means of production are concentrated. On the other side we find the proletariat as the class which has to find its subsistence by the sale of its labour power. Bourgeoisie and proletariat are the basic classes of capitalist society but not necessarily the only ones. Other classes such as intermediate sections, in various combinations may exist. But capitalism is possible only if there is a class of owners on the one hand, and a class of non-owners on the other hand. Secondly, it is the relationship to the means of production, which characterises these classes: ownership/control and non-ownership. It is not simply a question of rich and poor. Not all poor people are workers. They may be petty artisans, or hawkers, or peasants who still own some piece of land. An industrial worker may earn more, and yet he is a member of the working class whereas the poor peasant-owner is not.

The working class is not homogeneous. It consists of various sections, skilled and unskilled, on daily wages or on monthly pay, under the poverty line and well above it. What unites them is that they are all forced to sell their

labour power, be it under different conditions. A working class crosses the border-line of the working class only when his salary allows him to set up his own shop, to become a petty money-lender or to start living or renting out houses etc.

13.5 Expansion of Markets and Production

A further pre-condition for the development of capitalism is the expansion of the market. Pre-capitalist small-scale commodity production works for a limited market. In the 16th C, a commercial revolution took place in Europe. Discoveries of new trade routes opened the Vasco-da-Gama era of world-wide trade under colonial conditions. The expansion of the market encouraged large-scale production and thus the growth of capitalism.

The capitalist entrepreneurs can emerge only when a certain scale of production has been reached. The guild master and his limited number of journey-men and apprentices do not produce enough for setting the master free to do only the directing and supervising work. The capitalist as director of an enterprise emerges with the scale of production growing larger.

a) The Production of Surplus Value

With the market for commodity-production expanding and with a minimum of capital in the hands of a class of owners of the means of production and with a sufficient number of workers ready to be hired on the labour market, capitalist production can develop. Once it has gathered momentum it has its own internal dynamism to expand further and further. Marx calls it the "restless never-ending process of profit-making". How does it work? The key answer of Marx is his theory of the production of surplus value.

Box 13.3: The Capitalist Entrepreneur

Capital is formed when money ceases to be only a means of exchange, which facilitates the exchange of commodities and when the increase of money, adding new value, becomes the aim of economic transactions. The user and the merchant try to achieve this in the sphere of the market. The capitalist entrepreneur does it by subordinating the process of production itself to this purpose. He buys raw materials, means of labour, etc., and he buys labour-power. The labourers are paid for the use, for the consumption of their labour-power by wages. The owner of the means of production appropriates their products. After selling them, he has made a profit. Where does this additional money come from? Has money the power, to create more money? Is it the shrewdness of the capitalist? Of course, occasionally there may be a windfall through a shrewd operation. But that does not explain the general process of profit-making. There are occasional setbacks as well for various reasons. Marx finds the course of profit hidden in one particular commodity which the capitalist buys on the market. The commodity is labour-power.

For Marx the extraction of unpaid surplus-labour is the key to understand the different forms of society: rent paid to the landlord in feudal society, taxes paid to the state in Asiatic society. These forms are connected with different political structures, needed to enforce this extraction. In capitalist society the appropriation of surplus-value happens in a new way. It is no longer the unpaid labour of slaves or serfs but the unpaid labour of wage-labourers. Workers in capitalist society receive wages. It seems they are

paid for their work. That is the great mystification in capitalism which covers up the process of exploitation. Actually, they are paid not for their work but for the use of their labour-power. What they produce is worth more than their wages. The wages cover only the cost of necessary labour, that what is needed to maintain the labourer. The value of what he produces is more than that. The Capitalist appropriates the difference, which is the surplus. This is possible because labour-power is a commodity, which can be bought on the market.

b) The never-ending process of profit-making

Capitalist tries to increase the rate of surplus value all the time. Now we raise the question why the capitalist has to be involved in such a restless manner in profit-making. This can be attributed to the unlimited greed, which is fostered by capitalism. But this greed should not be understood in a moralistic manner. But as capitalists, the process of accumulating capital will continue, otherwise they go bankrupt. This pressure comes from the competition between the individual capitalists which is characteristic of capitalism.

If a capitalist does not invest in new technology, if he does not expand production, others will move ahead and conquer the market and he will be left out in the cold. He cannot appropriate profit for his own consumption only or spend it just for some unproductive purposes. He must take part of it and put it aside for reinvestment. That part becomes new additional capital. Thus he has to accumulate capital. This implies the trend towards the concentration of capital in large-scale production. This concentration again becomes the basis for the centralisation of the ownership and control of capital in the hands of a few.

Reflection and Action 13.2

What is the role of new technology in capitalist production? Does it alter ownership and control of capital?

The market is like the jungle with its law of survival of the fittest. The general tendency is towards the elimination of the smaller one, to the centralisation of capital. The bigger capitalists grow bigger and fewer. We now consider what effect the law of accumulation of capital has on labour. Accumulation of capital means an increased demand for labour-power. This could lead to a rise in the price of labour. On a modest scale wages may rise for a while. But this does not change the basic position of the labourer, who is completely dependent on the capitalist. Capitalism does not only create demand for labour, it also creates unemployment through the process of mechanisation. In this way it creates an "industrial reserve army" of unemployed whose existence makes it possible for the capitalists to keep the wages of the employed under control. "The action of the law of supply and demand of labour on this basis completes the despotism of capital".

There is another reason why the capitalist has to expand production unlimited. In the process of accumulation of capital the proportion of constant capital increases and becomes greater in relation to variable capital. This is called the growth in the organic composition of capital. Since the constant capital increases in the process of mechanisation and the part of surplus value producing variable capital becomes relatively less, Marx assumes a "tendency

of the average rate of profit to decline". The more a capitalist expands the lower his rate of profit becomes. He can only make good for it by expanding the scale of production.

But the ever increasing expansion of capitalist production leads to inevitably to an economic crisis. That is the other law of capitalism which, Marx establishes. These crises are the result of the basic contradiction between capital and labour. In order to survive capital must accumulate and expand. For its expanding mass-production it must find masses of buyers. These masses consist to a large extent of workers. They can only buy if they receive higher wages. But higher wages reduce the capitalists' rate of profit. Every individual capitalist, therefore, would like to keep his own workers poor, and to see the rest of the workers rich enough to buy his products.

13.6 Monopoly Capitalism and Imperialism

The dynamism of capitalism, the permanent pressure to accumulate capital, leads to a change in the character of capitalist economy. The era of free competition brought about a tremendous expansion of productive forces and of production on a mass scale. But this led simultaneously to the concentration and centralisation of capital, and thus to a new situation in which a decreasing number of big companies or groups of companies were able to conquer monopoly positions in the market. Monopoly capitalism developed through cartels, trusts, holdings and fusions, capitalists move to protect the rate of profit against the effects of free competition. Once the market is under monopoly control higher profits can be achieved by limiting production instead of increasing it, by holding back technological improvements instead of introducing them, by lowering the quality of products instead of rising it. Marx foresaw the rise of monopolies as the result of the concentration of capital. But monopoly capitalism became dominant only after Marx's death.

Several Marxists tried to provide a theoretical framework for the analysis of this new phase of capitalism. The Austrian Marxist Rudolf Hilferding published his study "Finance Capital – the latest phase of capitalist development" in 1910. The Polish-German Marxist Rosa Luxemburg came out with her study "The accumulation of Capital" in 1913. The Russian Marxist N Bukharin finished his "Imperialism and World Economy" in 1915. And Lenin completed his "Imperialism, the highest stage of Capitalism" in 1916.

Lenin made use both of Hilferding and Bukharin, though he differed on certain points with them. For example, he did not agree with Hilferding that monopolisation would eliminate all free competition within a national economy.

Box 13.4: Basic Features of Imperialism

- The concentration of production and capital has developed to such a high stage that it has created monopolies which play a decisive role in economic life.
- The merging of bank capital with industrial capital, and the creation, on the basis of this 'finance capital', of a financial oligarchy;
- The export of capital as distinguished from the export of commodities acquires exceptional importance;
- The formation of international monopolist capitalist associations which share the world among themselves; and
- The territorial division of the whole world among the biggest capitalist powers is completed.

13.7 Conclusion

The origins and development of capitalism has been traced and understood by various social thinkers based on different parameters. However, Marx's understanding of Capitalism has influenced greatly than any other theories. The main argument by Marx is that feudal mode of production has been replaced by capitalist mode of production. And under capitalism, society is divided into two main antagonistic classes – the class of capitalists or bourgeoisie and the class of proletariats. The main economic law and the stimulus of the capitalist mode of production is the creation of surplus value by the workers and its appropriation. The unpaid labour of wage workers is the source of surplus value.

13.8 Further Reading

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Giddens Anthony 1971. *Capitalism and Modern Social Theory*. Cambridge University Press.

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