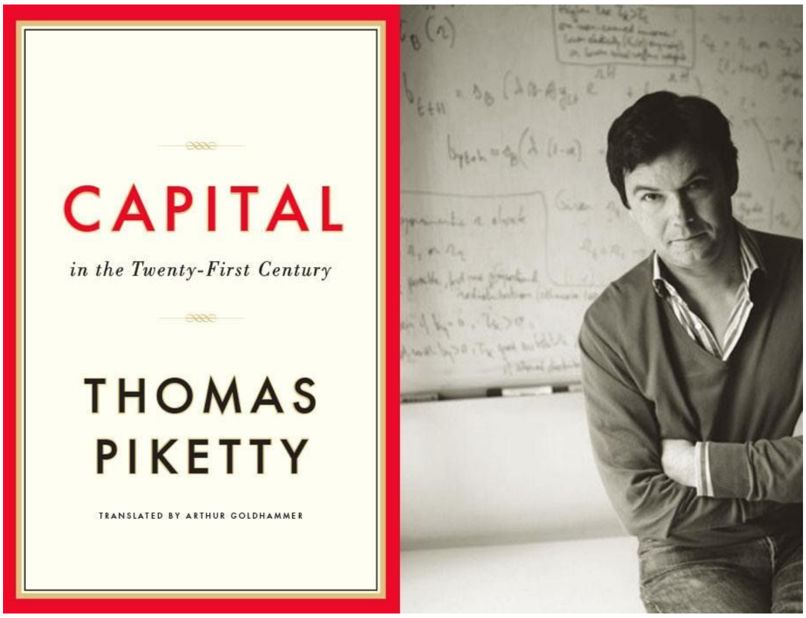
• ECONOMICS •

Review: Piketty on Malthus, Ricardo, Marx and the Comeback of Capital

Kaveesh Naggea, *Mauritius*



In his sweeping work Capital in the 21st Century, French economist Thomas Piketty narrates the historical evolution of capital, its nature and structures, and the socio-economic and political implications of that evolution. One cannot give a fair account of this mammoth work (firmly grounded in data series) in one go. Let me begin by describing the ways in which Piketty analyzes the influence of three great thinkers of the 18th and 19th centuries: Malthus, Ricardo, and Marx. Here is an overview of what he tells us:

Classical economy, Piketty tells us, was born in England and France in the late 18th and early 19th centuries. This was a time of drastic change, owing to demographic growth, a massive rural exodus, and the Industrial Revolution. British economist Thomas Malthus contended that the impending and major threat of his time was overpopulation. Working on the accounts of Thomas Young of pre-revolutionary France (which was then the most populous country in Europe with a 30 million-strong population), Malthus took notice of the fact that this demographic explosion had contributed to the stagnation of agricultural wages and an increase in land rents until the eve of the Revolution. The mass poverty Young described in his diary led Malthus to argue in favour of cutting all welfare to the poor in Britain and of monitoring reproduction of the poorer classes, so as to eschew societal ruin. Admittedly, those dire prophecies were tinged with the fear that pervaded European elites in the light of the great socio-political upheavals of the late 18th century.

Piketty goes on to examine the theories of British economist David Ricardo who was interested in the evolution of land prices and land rents and published his analyses in 1817, in a book entitled *Principles of Political Economy and Taxation*. In it, he prophesied that land rents would increase continuously as both population and output would grow. Landlords would therefore grow richer and claim an increasing share of national income (as opposed to other forms of income, for ex. income from labour), which would destabilize society and therefore call for higher rent taxes. This is called (known) the scarcity principle. However, Ricardo did not account for technological progress and the industrial revolution, which triggered farmland prices to plummet. It remains, however, that his scarcity principle stays relevant to the modern world. In our day, urban real estate for example, as well as oil reserves, both enjoy high demand and the owners of those assets could claim ever greater shares of income, resulting in greater inequality and social tension.

Marx's theories are a reflection of the socio-economic backdrop of his time: one of flourishing industrial capitalism. One cogent fact was the miserable condition of the proletariat, the workers, socially valued only by their labour-power, who flocked in a great exodus to the cities and were crammed into urban slums. Indeed, Piketty notes that the purchasing power of wages only started to grow in the latter half of the 19th century. It was a time of significant economic growth which translated into an increase in the share of income from capital. In other words, the capitalists and shareholders were reaping all the benefits of growth while wages stagnated until the cataclysm of World War One reduced this stark inequality. In the same year as the Spring of Nations, Marx published the Communist Manifesto where he dismissed the 'bourgeois economists' (who 'saw the market as a self-regulated system [...] in accordance with Adam Smith's 'invisible hand' and Jean-Baptiste Say`s law') and Proudhonians (see *Pierre Joseph Proudhon*, founder of *Mutualism*). Marx reused Ricardian thoughts on the price of capital and his principle of scarcity to assert that the accumulation of capital (machines, factories etc.) by capitalists had no limit: hence what some economists call the 'law of infinite accumulation'. According to Marx, this concentration of capital would lead to the subversion of the capitalist system, in two distinct scenarios:

first, 'violent conflict among capitalists' (Piketty takes the example of the Franco-German tensions over colonization of Morocco in the early 20th century) if the capitalist accumulation leads to a decrease in the rate of profit (hence killing the whole process of accumulation), or, if the rate of return doesn`t plummet, the capitalists` share of national income (and therefore inequality) would grow so great as to lead to a workers` revolution, as evidenced by the accounting identity below:

$$\alpha = \mathbf{r} \times \beta$$

Reading: α the share of income from capital in national income, r the return on capital (r is bound to decrease as β increases) and β the ratio of the value of all existing capital over national yearly income, effectively gives the total existing amount of capital). As you can see, if the capital stock increases more rapidly than the return r decreases, the capital share of income α will increase indefinitely, otherwise if r decreases so rapidly as to cancel the increase in B, or surpass it, capital's share of income a would either stagnate or plummet respectively, leading the capitalists to wage war against each other: it is unclear, however, whether Piketty means that the capital share would need to remain constant or decline in order to provoke this kind of internecine capitalist conflict)

However, Marx failed to account for structural growth enabled by technological progress. Admittedly, in a regime of extremely low growth, this Marxian scenario of accumulation and super-unequal society is possible: as g nears zero, β (capital/income ratio, or capital stock) tends towards infinity, as evidenced by the asymptotic law below. But in reality, structural growth offsets that effect.

$$\beta = \mathbf{s/g}$$

(Where s is the savings rate and g is the long-term structural growth rate, i.e. the sum of productivity growth and population growth).

Marx, in fact, did not have access to adequate statistical series and neglected an overall analysis (across all sectors of the British economy) of capitalism. Piketty notices, however, how those inner 'contradictions' of capitalism that Marx emphasized help explain capital accumulation (and spikes in inequality) during regimes of slow growth. This study illuminates the fact (brought forward by Piketty) that the capital/income ratio today has risen (after a steep decline during the 2 world wars) to six years of national income (levels last seen during the Belle Époque). Piketty says that the capital share of income α will likely increase as a result, exacerbating inequalities as most of the return on capital accrues to a small group of people: in 2010, 50% of total income in the US (whether capital- or labour-derived) accrued to the top decile (whose income is mostly derived from capital, usually stocks), compared to 35% of total income in 1970.

One can see, therefore, how this historical study of capitalism and wealth (or capital) distribution cast a light on the origins of contemporary evolutions of capitalism towards higher concentration of capital, and ultimately higher inequality, and help us anticipate the social and political repercussions that might follow.

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