

# CAPITALISM REBORN

By

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## Preface

For the past 250 years, the world has been blessed with astonishing progress. Economic well-being has improved throughout the globe. No more than 10% of the world's people now live in abject poverty vs. well over half in the 18<sup>th</sup> century. Life spans have exploded; before 1800, most people lived fewer than 50 years, while in the developed world today an average person can contemplate more than 75 years of a reasonably healthy life. Most people improved their economic lots more or less equally over those two- and- a- half centuries.

However, in the past 40-50 years, income inequality within many countries has grown exponentially, with the top 10% of workers in the US keeping about 90% of all gains in both incomes and wealth since 1980. And as growth in developing countries spurted, so did income inequality. The contrast between GDP numbers (very positive over the past five decades) and income inequality (very negative, for those not in the top 10% of the population) is stark. At the same time, discontent with the economic and political systems that encouraged these disparities has shot up, with the most recent survey in the US noting that less than 40% of people expressed trust in government.

Both these observations are true. How do we explain the contrast between the very long-term picture, which appears so bright, and the more recent period, which is relatively disappointing?

It is capitalism that is responsible for this contrast. But it is not the same capitalism in both periods. We must therefore define what we mean by capitalism, in its different forms. Capitalism is not monolithic; there are at least four varieties which we will discuss. It started with democratic market capitalism in the 18<sup>th</sup> century, morphed into laissez-faire capitalism for much of the 19<sup>th</sup> century, evolved into crony capitalism in the late 19<sup>th</sup> century, and featured a return to democratic market capitalism from about 1910 until the late 1960s and early 1970s. Since that time, the US re-adopted laissez-faire capitalism with a vengeance, ending in the last few years with a noticeable turn towards cronyism. Countries such as Russia and China have more recently adopted autocratic capitalism, a relatively new form combining ultimate state control with partial but restricted freedom for private business.

We will define each variety of capitalism, and the circumstances in which each form arose. And we will contrast capitalism with socialism, both socialism as it was conceived and as it has been practiced.

Today, we are at a crossroads. Do we continue towards greater income and wealth disparities, or do we try for fairer outcomes? Looking hard at the past, especially in the US, we will see that major changes have happened; greater equality can co-exist with more than adequate increases in overall wealth. Having done it before, can we do the same again? What are the major differences between the early 20<sup>th</sup> century (when we shifted to democratic market capitalism) and today? Can the same forces that brought about change in 1910 be counted on now? If we are successful, there is the promise of both a return to eventual political and economic harmony and to the solution of what appear to be intractable problems such as climate change. [note 1]

## I. Beginnings

While capitalism emerged slowly out of feudalism, it was not proclaimed as a useful doctrine until 1776, when Adam Smith published *The Wealth of Nations*. This was his second book, as Smith had already written a much read and widely praised study of human psychology, ethics and morals, *The Theory of Moral Sentiments*. That book stated what were for Smith certain immutable truths, among them being:

- a) Self-love is the deepest human passion, but it is balanced by a desire to help others, and by a desire to receive praise for doing so.
- b) Sympathy [we would use the word “empathy” today] is the principle on which humans must depend; when we agree with the emotions of another person, we naturally feel sympathetic to them.
- c) Humans have an unfortunate tendency to admire and emulate the rich and famous, which we must try to contain.

This was Smith’s majestic attempt to provide an understanding of human nature, as a foundation for life. To quote a biographer of Smith: “In *The Theory of Moral Sentiments*, Smith offered a powerful conjecture about the nature of the civilizing process, about the ways in which ordinary human beings engaged in the business of ordinary life set out to satisfy their moral needs, and about the way in which some citizens acquire that sense of fitness and ethical beauty which makes it possible for them to aspire to a life of virtue.” [note 2] Another scholar of Adam Smith summarizes *The Theory of Moral Sentiments* as follows: “Smith frequently returns to the idea that we are by nature often led in two very different directions. On the one hand, we are naturally led to be concerned with ourselves and our own wellbeing. On the other hand, we are naturally led to be concerned with the wellbeing and happiness of others. Both our nature and the nature of our world pull us in different directions.” [note 3]

Smith then turned his attention to commercial society in *The Wealth of Nations*. Here he introduced the concept of the division of labor (many people doing just one thing well can produce more units than a group in which each member tries to do everything). He elaborated on the principal of “the invisible hand,” by which self-interest can serve society, even if the individual does not realize that he/she is doing so. He was a strong advocate for individuals being able to employ capital in any venture that satisfied the rules of society. And he was a passionate advocate of free trade between nations, provided that all parties recognized similar rules of law, and provided that countries with highly paid labor and with relatively high costs of production had to very gradually phase in trade with a low-cost country, to give domestic industries time to adjust. He then added other crucial concepts to satisfy his moral principles:

- a) The poor have every right to as good an education as the well-off; women have as much right to education as men
- b) Monopolies are the worst form of government or organization yet devised.
- d) All people like to advance in the world, and their self-interest can be an unwitting but important channel to advance not only a person’s wealth but that of society as a whole.
- e) Society must have respect for laws, which the government must also abide by.

He also cautions that self-interest can be destructive, and that rules of law and fairness must check our selfish interests before they get out of control. He sums up by saying that there are three great principles of a successful commercial society: liberty, justice and equality. Liberty means granting to individuals the right to a free market in which to sell their goods, guaranteed by a freely elected government that maintains overall order through just laws and occasional regulations. Individual freedom was the overarching principle, but it had to be modified by laws and customs, because the interests of society as a whole had to be supreme. Smith recognized that human nature would have to be restrained for both equality and justice to triumph, and it is a crucial part of his theories that tensions between these three principles are always present.

I refer to Smith's vision as democratic market capitalism. A free market must go hand-in-hand with a free and democratic government (of course, in his day, the laws only permitted men of property to vote, but within that constriction, democracy was far better than any other alternative). But self-interest must be subject to the objectives and restraints of society as a whole.

Another vision of capitalism arose in France in the late 18<sup>th</sup> and early 19<sup>th</sup> centuries, that of *laissez-faire*. This was basically a simplified version of democratic market capitalism, with few if any rules to check the self-interest of the businessman. The free market was to rule supreme, as government would only hinder and unfairly restrict the vast productivity and imagination of the individual. Regulations were to be avoided, and laws were there simply to help advance the liberty and protect the property of the individual. There was an assumption that, somehow, all this self-interest would automatically be a great good for society. This theory paid little if any attention to Smith's cautions about the conflicting interests of liberty vs. justice and equality. Smith unfortunately is referred to, in several history books, as a believer in *laissez-faire*. That is an error. He always advocated the interests of society and knew that the tensions between rank self-interest and the advancement of the people as a whole had to be eventually resolved in the favor of the greater good. He railed against the monopolies and the mercantilist policies of the 18<sup>th</sup> century. He knew that monopolies were always a means to create vast private wealth with no regard to the general interests of the common good; and he realized that a mercantilist policy of forcing colonies to sell raw materials on the cheap to the home country, which then exported high-priced manufactured goods back to the impoverished colonies, was unjust and reason for colonies, such as those in America, to rightfully revolt.

Smith also fully recognized the vital role that government can and must play in the establishment of free markets. As another biographer of Smith notes: "Far from always being choked back by rules and law, markets vividly illustrate how personal freedom and prosperity can be enlarged by them. Far from being intrinsically opposed, states and markets rely on and benefit from each other. Provided they are legitimate and legal, markets generally have public as well as private value." [note 4]

Adam Smith's philosophies about markets and human nature can be summed up as follows: "The real Adam Smith was not an advocate of self-interest, did not believe rational behavior as constitutes solely by the pursuit of profit, was not a believer in *laissez-faire*, and was not pro-rich. Nor was he anti-government, although he shows a deep understanding of its limitations and

scope for possible abuse. It is precisely because of his belief that commercial society reflects and can assist the development of ‘natural liberty’, and can enable human well-being and freedom to flourish—indeed to flourish better than other forms of political-economic self-organization permit—that Smith values commercial society.” [note 5]

However, the overall simplicity of laissez-faire had considerable appeal. The nuances of Smith’s observations, and his warning about the tensions between the individual and society, were laid aside. Monopolies, if they existed, were there for a perfectly good reason--efficiency. And if mercantilist policies disadvantaged colonies, so much the better for the home country. The role of the state was just to get out of the way. Laissez-faire did not ignore ethical standards, but the adherents of laissez-faire made the heroic assumption that all this self-interest would somehow conform to those standards.

In the early 19<sup>th</sup> century, laissez-faire made considerable progress, especially in the US where popular textbooks of the time, written by Protestant clergymen, praised the virtues of unimpeded capitalism. In 1837, Francis Wayland, a Baptist minister and president of Brown University, published *The Elements of Political Economy*, by far the most widely read and popular economics textbook pre-Civil War. He defended free enterprise and free trade as being justified by God’s laws, as being “an expression of God’s unity and perfection, no less than the laws governing the physical universe. “[note 6] Francis Bowen, the editor of the “North American Review,” backed up much of what Wayland said, except for the fact that he advocated for a protective tariff to assist domestic manufacturers. He defended the doctrine of laissez-faire as follows: “Laissez-faire: these things regulate themselves, in common phrase; which means, of course, that God regulates them by his general laws, which always, in the long run, work to good.” [note 7]

Of course, in the era before the Civil War, much of business initially was done by small companies with relatively few employees. This model was giving way to an emphasis on large companies, especially in the Northern states, as we approached the 1860s. And the Civil War showed that the industrial age, with its great efficiencies and productivity, was vastly more effective than an agrarian society, which had to rely on unpaid slave labor.

After the Civil War, the industrial age exploded. Railroads, basic industries such as steel, textiles, and later on oil, all grew rapidly and without restrictions of any kind. This era of exploitive capitalism was described by Mark Twain in a novel published in 1873. Entitled *The Gilded Age*, it was a satire of the greed, corruption and selfishness of the period from roughly 1870 to 1905. The title of the book was later adopted to characterize that time period.

In 1893, the world came to Chicago, which celebrated the Columbian Exposition, a massive display of American power and industrial might. Henry Adams, an acute observer of the American social scene as portrayed in his autobiography *The Education of Henry Adams*, felt that “The Fair’s authentic nature could be found in the dynamos and steam engines that he discovered in one of its vast exhibition halls. These impressive machines...pointed to an American future far removed from the simple agrarian republic, now in its death throes.” [note 8] Industry, and not the industry of small, simple business such as dominated before the Civil War,

but really big and impersonal business, was moving quickly into major importance. Such a massive expansion of industry put pressure on a banking system that was still suited to the earlier model of small companies with managements known to the banker personally.

Two enormous banking failures hit the US, one in 1873 and another one twenty years later. The first, caused by the failure of the Northern Pacific Railroad, produced a depression that lasted six years. The second was virtually as bad, as noted by the author of the recent biography of Henry Adams: “Prompted by the January bankruptcy of the Philadelphia and Reading Railroad and followed by over the next few months by the insolvencies of several other key lines, the economy shed nearly six hundred banks and fifteen thousand businesses while unemployment exceeded over 40% in some areas.” [note 9]. The contrast between the exciting glitter of Chicago’s White City and the four-year depression that started, ironically, also in 1893, sums up the bitter contrasts of the Gilded Age.

The bank failures and resulting depressions were symbol of the changes wrought to democratic market capitalism. They were a fundamental part of our shift to what I refer to as crony capitalism.

## **II. Crony Capitalism in the Gilded Age**

Starting with the administration of President Ulysses S. Grant, both the public and the private sectors of the US economy and political system were run by a relatively small tier of men, with little sense of morality but with great ambitions. Grant himself, an effective president with a high sense of morality, could do little against the corruption of his advisors and cabinet. And the relatively weak presidents who succeeded him often found themselves in the hands of big-city bosses, such as Tweed (New York) and Hanna (Cleveland).

The corruption and the cynicism of the politicians of the Gilded Age were matched by the rapacity and extreme selfishness of the industrialists. This was laissez-faire capitalism but with hardly any checks on the pure pursuit of self-interest. So, it became a symbol of yet a different and more extreme form of capitalism--crony capitalism.

Here is a description of the Gilded Age in its particulars:

- 1) “Huge advances in communication, transportation, and standards of living have brought to almost all Americans a degree of material well-being unmatched in our history. And yet this prosperity has come at a cost. While industries spawned by technological advance have allowed huge corporations to produce unparalleled profits, very little of this wealth has trickled down. Extremes of wealth and poverty are everywhere on display. “
- 2) “Corporate monopolies have hoarded profits and gained unrivaled economic influence through a wave of mergers. Workers’ leverage has eroded, and capitalists cite their responsibility to shareholders and market forces as justification for keeping pay low. The economic well-being of the middle class is eroding and soaring private debt has become a common buttress to lagging incomes. “

- 3) “Politicians collect exorbitant amounts of money from wealthy donors which they use to win elections, creating a dangerous mutuality between wealth and power. “
- 4) “Inadequate regulation further fuels an irresponsible use of America’s vast natural resources. “
- 5) “Many of the corporate titans who dominate the American imagination live by an ideology of individualism that barely masks selfishness and an air of superiority. The pursuit of unfettered self-interest is considered a laudable ethic to live by. A drift towards self-centeredness in private life is matched in the public square. Public debates are characterized not by deliberation on differing ideas, but by demonization of those on the opposing side. The result is a nation more and more fragmented along economic, ideological, racial and ethnic lines. A rising tide of populism has captured the enthusiasm of many, especially in rural areas.” [note 10]

Remember that this describes a period of about 120-140 years ago! But the parallels to today are uncanny: “Throughout the Gilded Age, the specters of poverty and oppression waited on the banquet of expansion and opportunity.” [note 11] And continuing: “Instead of jealously husbanding their investment in human capital, business owners squandered it prodigally, seemingly bent on, one way or another, working their employees to death. They did this in two ways—first, through wages compatible only with abject poverty and, second, by providing working conditions which threatened life itself. [note 12] The working poor were not only poor, they had very short lives, and nobody seemed to care.

Crony capitalism exults in the triumph of utter selfishness and individuality, at the expense of the general good of society. Crony capitalism results in enormous gaps of both income and wealth between the top 5-10% and the remainder of the population. In 1913, the end of the Gilded Age, the richest 1% of the US population received 20% of the nation’s overall income (a figure not approached again until 2014) and owned just under 50% of the nation’s wealth.

Every age has to find intellectual thinkers who both justify and personify the extreme characteristics of that age. In the late 19<sup>th</sup> century, a doctrine termed Social Darwinism was used to justify vast extremes. Certain thinkers, overwhelmed by the logic of Darwin’s great book on the origin of species, went much further than Darwin himself and pointed towards the success of the very few as totally justified by culling out of the weak. That might be very tough on those who fail to rise but the ones who do rise will always do so by their superior intellect and drive. It is truly survival of the fittest. A renowned American sociologist of the period was William Graham Sumner. He is quoted as follows [note 13]: “Some people were better at the contest of life than others...The good ones climbed out of the jungle of savagery and passed their talents to their offspring who climbed still higher...Attempts to overrule evolution—as by alleviating the plight of the poor—were both immoral and imprudent.” This insolent and uncaring attitude was generally reflective of that era. Even a number of distinguished clergymen echoed these doctrines. Henry Ward Beecher, the brother of Harriet Beecher Stowe (author of *Uncle Tom’s Cabin*), was the best-paid minister just after the Civil War. He made it a point to equate riches with goodness: “Nowhere else does wealth so directly point towards virtue in morality, and spirituality in religion, as in America.” [note 14] And the famous rector of Trinity Church of

Boston, Phillips Brooks, who served in the late 19<sup>th</sup> century (and outside of which church there still stands a larger-than-life-size statue of the rector), stated : ”The instinct which asks for equality is a low one. Equality, if it were completely brought about, would furnish play only for the lower instincts and impulses of man. It is the fact of privilege, the inequalities among men for which they do not seem to be responsible, which makes a large part of the interest and richness of human existence.” [note 15]

Such an attitude, of course, was not restricted to thinkers of the 19<sup>th</sup> century. Milton Friedman, a highly influential economist of the mid-20<sup>th</sup> century, is quoted as follows: “The closest approach that the United States has had to free enterprise capitalism was in the nineteenth century. Anybody was free to put up an enterprise, anybody was free to come to this country...it was a period in which the ordinary man experienced the greatest rise in his standard of living that was probably ever experienced in a comparable period in any country at any time.” [note 16] Hyperbole aside, Friedman’s conclusions are both accurate, as far as they go, and disturbingly narrow. He takes no notice of the well-known and enormous disparities of wealth; he takes no notice of the deplorable living standards in all of America’s big cities; and he takes no notice of the selfish grasping of power by the giants of industry (such as Rockefeller and Carnegie), as they form what they term “trusts”, the greatest monopolies and conglomerations of industrial power ever seen in this country.

In summary: “The Gilded Age had brought great material advance to America, but it had also brought inequality, polarization, social disarray, and cultural self-centeredness.” [note 17]

### **III. The Progressive Era, 1915-1970**

In the early years of the 20<sup>th</sup> century revulsion towards the vanities of the Gilded Age brought about convulsive changes. Crony capitalism eventually gave way to a resumption of democratic market capitalism.

The media of the day were one source of this change. Media, of course, then meant print. And magazines were very popular and widely read. Writers such as the muckrakers of the late 1890s described in excruciating and horrifying detail the squalid living conditions of the tenements of the big cities, the sweatshops, and the factory floors. Books were written by authors such as Ida Tarbell and Upton Sinclair to popularize the viciousness of the huge trusts in such industries as oil, meat packing, steel and the like. All these publications had growing influence on popular opinion.

Religious views also changed dramatically. Key churchmen began to call on society to recognize extremes of inequality, and to effect change. Washington Gladden, a Congregationalist minister in Columbus, Ohio, wrote a series of books to spur Christianity to address social ills: “The problem now before us [he wrote in 1893] is whether any higher power can be invoked to save the good that the greed of gain has brought forth upon the earth. This is the problem that confronts those of us who labor for the christianization of society.” [note 18] He was the

forerunner of a movement, the Social Gospel Movement, which tried to adopt scientific principles for the ultimate perfection of mankind. Religion and science were to be linked together to correct the ills of the Gilded Age. An ordained Baptist minister, Walter Rauschenbusch, wrote many books on this challenge: “Men learned to make wealth much faster than they learned to distribute it justly. That is the great sin of modern humanity, and unless we repent, we shall perish by that sin.” [note 19] By the very early 1900s, the Social Gospel Movement had taken over most mainline Protestant churches, and Social Darwinism had given way. Public opinion had shifted dramatically towards a search for a more fair society.

But it takes a leader to grab hold of public opinion and force real and substantive change. Teddy Roosevelt, who succeeded William McKinley (the last of the political robber barons of that day), seized on this change and rode it to a series of political victories, which inspired new laws in areas such as anti-trust and labor conditions, laws that would have seemed out of the question a decade earlier.

The Gilded Age was over. And democratic market capitalism made a comeback.

“In a decade or two at the turn of the twentieth century the Progressive movement—diverse in its politics, its demographics, and its ideologies and with little philosophic coherence except for a commitment to community—undertook initiatives that over time redirected the course of history.” [note 20]

Historians today refer to this period in the US as “the Great Leveling” or “the Great Convergence.” This was a period during which income equality made a surprising resurgence. Of course, two World Wars made a distinct impact, as did the Great Depression of the 1930s. Both wars and the depression forced a much different attitude of “we are all in this together,” and communitarianism (“we”) replaced raw individualism (“I”). As a result, the trend towards a more equal sharing of economic wealth began just before World War I, and it continued, with a brief delay in the 1920s, right through the 1960s. “What happened during the Great Leveling was much broader than just a decline in the top income shares. Inequality diminished even within the middle and lower ranks. And the Great Leveling was not just a manifestation of government’s redistribution from rich to poor with taxes and transfers. Incomes became more equal both before and after those taxes and transfers.” [note 21]

The share of the top 1% of richest Americans fell from nearly 20% in 1923 to 10% before taxes (8% after taxes) by the early 1970s. All this happened in six decades of very substantial and rapid growth in the US economy, interrupted of course by the Great Depression of the 1930s—but the very long-term trend shows remarkable growth, which was shared by every income segment in America. Actually, incomes of the lower economic classes grew much faster than those at the top, but from admittedly a very low base. Figures show that real income per family grew 21% over that period, but that for the bottom 99% it tripled: “In those decades we did not have to choose between growth and equality, as some economic theories have it—we were collectively richer and more equal. Mid-century America was hardly a paradise of perfect equality, but after more than sixty years of continuous progress, the chasm between opulence and penury of the first Gilded Age had been left behind.” [note 22]

Shares of wealth as well as income became much more equal too. In 1913, the wealthiest 1% owned 45% of the nation's wealth; that figure was cut in half, to 22%, by 1970.

The two Roosevelt presidents adopted policies that were primary contributors to both economic growth and equality. There was enormous investment in public education, supported enthusiastically by most Americans, right up to the 1970s. The labor union movement too gained many adherents; from 1897-1904, union membership grew to 14% of the workforce, not to go below that figure until after 1980. Actually, union membership grew steadily during the era of the Great Leveling, to a high of over 30% in the 1950s, before it began a slow but persistent decline, finally breaking below 20% in 1980.

Taxation was also a force for greater equality. Introduced in the early years of the 20<sup>th</sup> century, the federal income tax became more and more progressive, finally topping out in the 1960s. The estate tax, introduced in the early years of the 20<sup>th</sup> century, kept rising until it too topped out around the mid-1970s. Mostly middle-class entitlement programs, such as Social Security and Medicare, provided great benefits to the middle 40% of Americans, more than to either the top or lowest classes.

Teddy Roosevelt began the anti-trust movement, which continued unabated through the 1960s. Financial regulation was introduced primarily through the formation of the Federal Reserve System in 1913, and continued throughout the New Deal, with newly formed agencies such as the SEC (Securities and Exchange Commission).

Minimum wages were first introduced by states, and then were adopted on the national level in the 1930s. Once again, the minimum wage tracked closely the overall growth in incomes until the 1980s, providing a source of equality for the working class; after that date, it has fallen sharply, well behind the rate of inflation.

Both the Roosevelts embraced a sharing of wealth much more enthusiastically than most members of their economic class. Here is Teddy Roosevelt in a speech in 1910: "We grudge no man a fortune in civil life if it is honorably obtained and well used. It is not even enough that it should have been gained without doing damage to the community. We should permit it only to be gained so long as the gaining represents benefit to the community. This, I know, implies a policy of a far more active government interference with social and economic conditions in this country than we have yet had." [note 23]

Franklin Roosevelt went further than his distant cousin. His New Deal produced so many major reforms that it's difficult to enumerate them. But among them are Social Security, the National Labor Relations Act, the Tennessee Valley Authority, the National Housing Act, the Works Progress Administration, and the Fair Labor Standards Act. He was denounced many times by conservative, well-off people as "a traitor to his class," to which he replied with glee: "I welcome their hatred."

The Great Leveling continued under President Eisenhower, who succinctly stated: "Should any political party attempt to abolish social security, unemployment insurance, and eliminate labor laws and farm programs, you would not hear of that party again in our political history."

Eisenhower actually improved and strengthened many parts of the New Deal, through the creation of a new Department of Health, Education and Welfare; at the end of his two terms, social welfare spending as a percentage of GDP rose from 7.6% to 11.5% [note 24].

President Kennedy emphasized the communitarian ideals of that era. His inaugural address called on Americans not to ask what the government could do for them, but to ask what they could do for their country. So, right into the 1960s, the idea of “we” being more important than “I” prevailed for the country as a whole.

Minority rights lagged badly, however, during much of this period, until President Johnson introduced, and Congress passed, the Civil Rights Act of 1965. While many Blacks moved north in the 1920s-1940s (termed the Great Migration) to obtain manufacturing jobs in such cities as Chicago, Cleveland and Detroit, they were socially ostracized and housing remained mostly segregated. Still, minority incomes rose very sharply, because the base was so low, during the Great Leveling. Yet incomes for both minorities and for women generally remained far behind those of white men.

#### **IV. Crony Capitalism and the Return of Self-Interest**

The 1960s were a transition decade. A survey taken in 1960, for example, showed that 79% of Americans had great trust in government. But by the mid-1970s, that figure had dropped to 37%. The sixties ushered in a return of individualism vs. communitarianism, a breakdown of what had seemed to be an American compact to which most people subscribed, and challenges to American domination both economically and as a world leader politically. That these challenges were so serious and so effective produced a backlash.

The economic circumstances of the country changed radically in the 1960s and early 1970s, as did both political parties. There were five principal causes: the advent of global competition, the energy crisis, inflation, Vietnam, and Watergate. US industry and labor had enjoyed a true golden age from the end of WWII until the mid-1960s when the first really cheap and well-made products, such as autos, came from abroad and proved attractive to American consumers. Both industry and labor would have to become tougher and more competitive, an adjustment that fostered resentment and frustration. As we were importing vast amounts of oil from the Middle East, those countries formed a cartel (OPEC) to drive up prices very sharply, causing further frustration and angst. Then, partly because of the energy crisis and partly because of huge government deficit financing for the war in Vietnam, inflation soared. Finally, most Americans were disgusted by both the Vietnam War, which seemed interminable and pointless, and the Watergate scandal, which appeared to prove that even a president could be a scoundrel. In addition, in parts of the country, there was a severe backlash against civil rights. So, politics had to take cognizance of American discontent. The first party to do so was the Republican Party. It formed a new movement.

Every movement that wants to overturn previously accepted norms must have three important backers: ideologues, political converts, and very rich and dedicated followers willing to spend towards new goals.

In the late 1960s and early to mid-1970s, the Republican Party found these backers. There were three intellectuals, several politicians, and four or five billionaires.

The intellectuals were Milton Friedman, Robert Bork and Lewis Powell.

Milton Friedman started out as an economic theorist and historian of exceptional merit. It was he who brought monetary policy analysis to major importance more than 70 years ago. However, as he grew older his conservatism became more fixed, and he adopted highly simplified but persuasive economic positions. It was in September of 1970 that he published in “The New York Times Sunday Magazine” an article entitled “The Social Responsibility of Business Is to Increase Its Profits.” Bang! This shook the world of business, for up to that time most CEOs followed a model of stakeholder responsibility, with the stakeholders being customers, suppliers, employees, and shareholders, all of them being of more or less the same importance. CEOs believed it was the task of management to find a proper way between these conflicting interests, so that shareholders got a reasonable return, employees were paid a reasonable wage, customer goods were priced reasonably, and suppliers were paid a reasonable price. When Friedman said that only shareholder interests counted, suddenly this conclusion dominated business thinking like a storm. All of us prefer simple solutions to a complex problem. The solution may be wrong, but its very simplicity is what makes it so appealing. Here was a very simple idea that resonated with businessmen. No wonder it was adopted so quickly and effectively—effectively, that is, if you were a business owner or a shareholder. Profits as a percentage of GDP shot up in the succeeding decades while employee wage compensation declined almost as sharply. This was the first and probably most important manifestation of the crony capitalism and selfishness so marked in our economy for the past several decades.

Robert Bork was a jurist and a legal scholar who served from 1973-77 as solicitor general of the US, the leading lawyer of the Justice Department who argues cases before the Supreme Court. (Much later, in 1987, Bork’s nomination to the Supreme Court by President Reagan was turned down by the Senate.) He took it upon himself to eviscerate anti-trust policy. In 1978, he published *The Antitrust Paradox*, which stated essentially that there was only one test of antitrust—whether consumer prices rose. Gone were Adam Smith’s warnings of monopolies being bad in themselves, since innovation and competition could be stifled. According to Bork, if consumer prices did not rise, no one should care about a monopoly. Many scholars have since criticized Bork’s overly simplistic doctrine, noting that Congress, when it passed the Sherman Antitrust Act, had a much broader viewpoint than purely consumer welfare. But the damage was done. Courts adopted this simple test and anti-trust enforcement waned.

Finally, in 1971, Lewis Powell, a conservative jurist, wrote a now famous memo, entitled “Attack on American Free Enterprise System,” for the US Chamber of Commerce. It called for American business to defend its interests against all its critics (the memo enumerated college campuses, Ralph Nader, churches, the media, and intellectuals). It called for business to fight

back aggressively, through funding think tanks and legal organizations which could carry the fight to the courts. And indeed business did fight back, against all sorts of regulations that would in any way hinder the pursuit of profits.

Politicians were quick to seize on these new thoughts and premises. While the conservative wing of the Republican Party started up in earnest in the Goldwater era of the 1960s, it did not truly gain importance until somewhat later. Probably the politician who did the most to enlist support for these points of view was Speaker of the House Newt Gingrich, who both rallied the country to his side with what he termed a Contract for America, and who adopted Ronald Reagan as his way to get to the top. Reagan, whose sunny and optimistic attitude concealed a very conservative agenda, happily became the spokesperson.

But it always takes a lot of money to win elections. So up stepped several billionaires, led by Charles and David Koch, owners of the largest and most valuable privately owned company in this country. They were followed by other billionaires, such as Scaife and Olin. So now the Republican Party had what it wanted: intellectual leadership, political importance and plenty of money to spread this particular gospel. And Republicans in addition formed an alliance with the South, to lure people there who were both conservative economically and socially.

The stage was set for a return to selfishness greed, and cronyism. Our communitarian ideals, supported so well for the past several decades, vanished.

One observer notes: “Between 1980 and 2014 pretax national income grew by 61 percent. But the income of the poorest half grew by only one percent, while the income of the top 10 percent by 121 percent, and the income of the top 1 percent more than tripled.” The disparities of the Gilded Age reappeared. [note 25]

It is not correct, however, to regard this turn in American society as driven solely by economic events. There were huge changes in our cultural attitudes. We have to remember that, despite great advances from the end of WWII onward, there were large disparities between well-off whites and most minorities, and almost equally large disparities between male and female workers. These disparities began to boil over.

As the culture wars intensified, we saw a decline of communitarian spirit and the virtual disappearance of “the common good.” In 2020, the COVID crisis illustrated this all too well: “[The pandemic] appeared on the scene at a time of nearly unprecedented income inequality and partisan rancor. The same market-driven globalization project that had left the United States without access to the production of surgical masks and medications had deprived a great many working people of well-paying jobs and social esteem.” [note 26] The economic troubles of the lower middle class starting around 1980 can be tied in with cultural changes of the same period, a double blow to the cohesiveness and self-esteem of a group of people for whom the previous decades right after WWII had been a time of plenty and contentment. The cultural changes might have been far better absorbed had not the incomes of this class of people stagnated at a time when incomes and wealth of the elites skyrocketed. But “those who reaped the bounty of global markets, supply chains and capital flows had come to rely less and less on their fellow citizens, as producers and as consumers... As the winners of globalization pulled away from the losers,

they practiced their own kind of social distancing.” [note 27]. This attitude of scorn and disdain “helps explain why those left behind by globalization would become angry and resentful, and why they would be drawn to authoritarian populists who rail against elites and promise to reassert national borders with a vengeance. “[note 28]

Increasingly politics emphasized “identity” over the nation as a whole. Everyone determined to identify with a race, a gender, a sexual orientation, a religion, or a strictly defined geographical area. One group that did not fit into a simple category as neatly as others was that of a particular group, non-college educated and lower-middle class Americans, principally whites in the Middle West and the South. From the 1930s through much of the 1960s this group kept up well with economic progress. There were many jobs, especially in manufacturing and in extractive industries (such as coal, and oil and gas), available to people without a college education. Incomes were sufficient to provide for a typical family of four or five, and home lives were stable because of faith in religion and in small town values. But both cultural changes (the rise of minorities, of women, and of a plurality of religious and social visions) and economic changes (the impact of a flood of good quality and very cheap consumer goods from other countries especially China) dealt this class of Americans a series of body blows. On top of all these problems, most politicians paid little attention. Horrifyingly, this group fell prey to despair and cynicism, and became obsessed with drugs (opioids and heroin), drunkenness, and suicides. This became the only class of American citizens for which life spans actually fell from 1970 to the present day. [note 29] It is a very important and sobering reminder of the impact that may strike a country or part of a country when politicians make promises they cannot keep, such as implying that a flood of unanticipated competition will somehow lead to good for everyone. Crucially, of the 16 million jobs created from 2010 through 2019, only 3 million were for people without a college degree. So this forgotten class of citizens fell even further behind.

The election of 2016, and the resulting wave of white nationalism, came about basically because many of these people felt angry because they believed their concerns were ignored. How we could have done better is of course not an easy answer. Obviously, our country had a crucial priority to address the rights of minorities and women first. And it still has to make much greater progress for African Americans and other minority groups. Yet we should have paid attention to the statistics that portrayed in stark terms what was going wrong with this particular group of citizens left so far behind. The fact that we did not resulted in the election upset of 2016.

Every era ends often in a blaze, not of glory but of decadence. The Trump era brought crony capitalism to a high point, and its policies mirrored the Gilded Age. Selfishness was its hallmark, cynicism its calling card. Then, the acts of violence and of ignoring truth after the 2020 election summed up a troubling and tragic four years.

But a primary lesson of the period of 1910-1970 was how much progress was made towards much greater equality of incomes and wealth, and a much more communitarian and egalitarian spirit. No period is perfect, and the struggles of minorities and women showed how much better the nation could become. However, it was the reaction to that period, and the convulsive moves towards the “me” culture from the mid-1970s to today, which brought about the divisiveness and deplorable violence after the 2020 national election.

## V. Where Are We Now; What Can We Do?

The Trump era may mark the high point of selfishness and greed ushered in during the 1970s. It may mark the nadir of communitarianism. I say “may” for despite some positive signs, it’s too early to be sure.

Among the positive signs are a return to corporate stakeholder recognition as opposed to pure concentration on profits alone. In the summer of 2019, the Business Roundtable issued a statement, strongly endorsed by many corporate leaders, that business has responsibilities to our society, and that it fulfills those responsibilities by carefully considering all four stakeholders—shareholders, employees, suppliers, and customers.

Darren Walker, president of The Ford Foundation, gave an interview that summarized the views of many leaders of both for-profit and non-profit enterprises: “Friedman ignored that in a democratic-capitalist society, democracy must come first. ‘We the people’ grant businesses their license to operate--which they, in turn must earn and renew. I didn’t agree with Friedman then, and the decades since have only exposed his myopia. Just look where the obsession with maximizing profits for shareholders has brought us: terrible economic, racial and health inequities; the catastrophe of climate change. It’s no wonder that so many young people now believe that capitalism can’t deliver the equal, inclusive, sustainable future they want.”

While Walker glosses over the better economic efficiencies of a leaner corporation as well as the extraordinary entrepreneurial developments of US high tech, which were positive developments of the past 40-50 years, there is no question that much of his critique rings true. We must redefine capitalism in the way it was originally supposed to work: for the betterment of all, including importantly the poor and the middle class. We must return to a democratic market capitalism, to avoid the possible trap of the young turning towards the discredited idea of socialism.

Socialism may be defined as the ownership of all means of production by the state. It was first proposed by Karl Marx in the middle of the 19<sup>th</sup> century. He was shocked by the inequities of the industrial age, which he attributed to capitalism, especially private ownership. He therefore advanced the idea that the state should own all the means of production. Then, the citizens would share directly in the rise in the economy as they, rather than a small group of entrepreneurs and managers, would be the owners. Socialism, however, paid very little attention to the fundamental characteristics of human psychology, as so well described by Adam Smith. It ignored the fact that virtually everyone wants a chance to improve their lives through hard work and proper compensation, including a right to ownership. Also ignored was the crucial role of the price mechanism in displaying to private citizens their choices and their opportunities, as many prices were set arbitrarily by the state and not by market forces.

So when socialism was tried out in Soviet Russia, in post-WWII China, in smaller countries such as the Soviet Union satellites, in Cuba, and in other small countries in Central America, it failed. Growth suffered. All the riches of the society were concentrated in a small group of elite who commanded both the political and economic spheres, and left little to the vast populace. The

saying in Russia, as noted by an observer in the 1960s, is instructive: we pretend to work and they pretend to pay us.

Britain tried a fairer form of socialism after WWII, when the Labor Party nationalized much of British industry. While the government officials did not commandeer for themselves all the wealth of the country, such as in Russia, productivity and innovation suffered. When you remove most incentives for people to work, to start new companies and to grow their own businesses, the inevitable result is both very disappointing growth and plenty of inflation. Socialism was finally abandoned under a Conservative government in the 1980s, but the government's role in such services as housing, education and health care remained. Socialism was also the method of economic government in China until about the year 2000 and in Russia until about the late 1990s. When one looks at the very significant differences in well-being between West and East Germany and between North and South Korea, one can see so easily why socialism was a considered a colossal failure. Similar failures of today are such countries as Cuba, Nicaragua and Honduras, from which many refugees wish to flee. This is why the term socialism caused such upset and unrest in considerable parts of the American electorate in the 2020 election.

A mixed form of capitalism, where the means of production are firmly in the hands of private individuals, but which is modified by both laws and progressive government regulations, is practiced today by the Scandinavian countries, in which private ownership is matched by a very extensive safety net financed by high taxes. Unfortunately, these countries, as well as some of our politicians, refer to this as democratic socialism. No, not at all. This is a total misuse of the term "socialism." It rightfully should be termed capitalism but with a larger government-run safety net than in many other countries, as virtually all of the means of production remain under private ownership. Get rid of the word socialism and emphasize democratic fairness and compassion for all citizens, with capitalism in control but carefully regulated, and then you will have it right.

If it was the media together with a sharp change in religious attitudes that were basically responsible for public opinion changing from selfishness to a communitarian ideal in the early part of the 20<sup>th</sup> century, what are our chances for such a shift today? Certainly media—that is, social media—are much more a medium for baseless claims of conspiracies and election fraud than any of the magazines or popular authors at the start of the Progressive Era, which does not auger well. Likewise, the most popular churches of today, the evangelical Protestant churches, are mostly both socially and economically on the side of the "me" movement. Yet even in those churches, there are signs that the aftermath of the national election of 2020 has driven some important spokespeople away from the narrowness of their vision. It will take unafraid leaders with driving conviction to force more change in both social media and religion. In the meantime, we must start with a coming together of both business and government to restore democratic market capitalism. There are hopeful indicators this is happening. Operation Warp Speed was a highly successful alliance between private business and the federal government in the development of COVID vaccines, even if it took a change in administration in Washington to produce the vaccines efficiently. This could mark the end of the Reagan motto that the government is just there to hinder private individuals.

The case for a different approach to business and to democratic capitalism is finding recruits, especially in academia. For example: “The institutions that have historically held the market in balance—families, local communities, the great faith traditions, government, and even our shared sense of ourselves as a human community—are crumbling or even vilified.” [note 29] And the author continues: “For years, the proponents of the unchecked free market have been attacking government. But the alternative to strong, democratically controlled government is not the free market triumphant, but crony capitalism, a system where the rich and powerful run the state. There’s always a tradeoff, too much focus on the public good stifles the entrepreneurial dynamic which is the lifeblood of functional growth markets. Too much focus on economic freedom leads to the destruction of the social and natural world and to the degradation of the institutions that hold the market in balance.” [note 30] And “We will not reimagine capitalism unless we rediscover the values on which capitalism has always been based, and have the courage and the skill to integrate them into the day-to-day fabric of business.” [note 31] In truth, the author is signaling for a return to Adam Smith’s basic truths, morals, and value system.

The author’s consulting work with today’s newer business leaders shows that they desire to create returns for shareholders by taking a balanced view of what is going to produce good long-term growth: well-paid and properly motivated employees, fair consumer prices, concerns for diversity and involvement in societal needs, in addition to maintaining superiority in both technological and product development. There now are many examples in both American and international companies, which envision a return to a much better balanced world, where both government and business come together for purposes that benefit each other as well as society as a whole.

Summarizing: “This interplay between self-interest and a shared sense of the right thing is the energy that is propelling so many firms to explore the first four pieces of a reimaged capitalism—shared value, purpose-driven, rewired finance, and self-regulation—and is the reason I believe that they will increasingly support the fifth—the building of inclusive societies.” [note 32] While this vision may be a bit too idealistic and optimistic, I am hopeful it will eventually be proved correct.

Another appeal to business starts with a challenge combined with a warning: “Capitalism triumphed in the Cold War because it promised a better life for the majority of people around the world, and the improving conditions for many millions seemed to affirm its claim. But dramatically unequal access to capitalism’s benefits and mounting evidence of its collateral damage have cast doubt on that promise and provided grist for ideological naysayers to challenge its fundamental soundness as a basis for economic organization. We believe that time to deliver on the core promise of free-market capitalism is running out. If market capitalism cannot be made to work for almost everyone, then it will eventually not be allowed to work at all.” [note 33]

After listing and examining the disruptors of today—an unrestrained and at times unaccountable global financial system, a possible breakdown in trade and trading systems, economic inequality

and populism, immigration, environmental degradation, rise of state capitalism, terrorism, and inadequate funding of global health and education—the authors then cite a number of useful examples how a company’s self-interest can contribute to its own prosperity as well as assist society. JP Morgan Chase, for example, by investing heavily in the rebuilding of Detroit, provided jobs for that city and opportunities for the bank to improve its eventual profitability there. Cummins Engine built a world-class manufacturing center in Southeast Indiana, and invested in that area’s educational institutions and infrastructure, demonstrating that community health and company prosperity go hand-in-hand. Unilever announced in 2010 a highly ambitious plan to double its business in a decade while setting an equally ambitious set of both environmental and societal goals. By 2020, the plan had succeeded in all its environmental and social objectives, and the stock had risen 290 % over that time period. Private well-being and public well-being can go together. [note 34]

However, the most significant challenge to American political and economic leadership is that from countries with a new model of autocratic capitalism, particularly Russia and China. “Russia and China are the two most important examples of state capitalism...In the 1990s, with the breakup of the Soviet Union, Russia experienced considerable privatization. But beginning with Vladimir Putin’s first term, from 2000 to 2008, the economy has been under the tutelage of the Kremlin. Private ownership remains, but significant companies follow the leadership of the government or risk ceasing to be private.” [note 35] As the experience of certain oligarchs demonstrate, one must always obey the edicts of the Kremlin unflinchingly. Otherwise, you risk expropriation, exile or jail. In addition, Russia uses its exports, especially of oil and gas, as a weapon to advance its own interests. And as Europe depends on Russia for a significant portion of its energy needs, Russia can wield considerable power.

China is a greater challenge to Western concepts of capitalism and democracy than Russia. China, starting in 1979, opened itself to private ownership and encouraged entrepreneurs to start new companies, which for over 25 years proved enormously successful. In 2001, when China was admitted to the World Trade Organization, the West generally had naïve expectations that China would obey consensus rules of trade and finally adopt some of the trappings of democracy. That was not to be. China’s system has been a combination of State-Owned Enterprises (SOEs) and private companies. For a while, private businesses grew much faster and earned vastly more net income than SOEs. But when President Xi took over, policies changed. President Xi has reinstated the ultimate power of the SOEs and has insisted that key decisions be approved by him, cutting the egos and the ambitions of the Chinese private sector down to where they now bow to his every command. Whether this heavy hand will stifle the innovation that made private Chinese high-tech companies so successful in the past decade is yet to be seen.

Instead of having the price mechanism the primary means to enable businesses and citizens make carefully considered economic decisions, China relies as much on state edicts as on private enterprise. This system forces private business into cooperation with the Chinese Government on virtually every matter deemed of real import. And this system of some freedom for the private

sector but always subject to state control, is now being adopted by smaller countries such as Turkey, Hungary, and Poland. They have focused on what they perceive as the failures of democratic market capitalism, such as the vast income and wealth inequities in the US, the rapid rise of cronyism, the comparative neglect of such public spheres as education and public health, and the rise in populism that attacks democratic values. To those countries, autocratic capitalism seems to be a more impressive option than market or democratic freedom.

It is up to us to demonstrate to the world that a return to democratic market capitalism will produce not only good economic growth but a much fairer distribution of the spoils. If we can restore a proper balance between public and private needs, if we can recognize that all citizens need a fair break in both pre- and after-tax incomes, if we can restore a sense of “we are all in this together,” we can show other countries that a far less free model is far less attractive.

When we were faced in the early 1900s with a roughly similar challenge, we changed course, led both by public opinion and by inspirational leaders. That change of course—back to the ideals of democratic market capitalism—pulled us eventually towards a more just, more equal, and more satisfied society. And we enjoyed excellent growth in overall economic activity at the same time. Surely, if a majority of our citizens sees the need for and the attraction of this outcome, we can do it.

## **Summary**

Over 250 years, capitalism has triumphed. But its offshoots from democratic market capitalism—laissez-faire, cronyism, autocratic and authoritarian states—have produced disillusionment in much of the world in the past few decades. We in the US made several false choices since the 1970s. We drastically oversimplified both the definition of the responsibilities of business and the definition of anti-trust, and we changed the definition of public-private relationship from cooperation to antagonism. The result: class warfare between identity groups, huge disparities between income groups, vast concentration of wealth, and a feeling that “I” was much more important than “we”.

Can we regain our confidence, our respect for fairness, our desire to work towards a common ground? We did it before when it counted. Given a sense of good will (which today seems tough but certainly possible) and given leadership that stresses the unity of our purpose, we can do it again.

It’s time to start.

## NOTES

- 1) For sources, please see the Bibliography attached to this paper.
- 2) Phillipson, page 157
- 3) Hanley, pages 7-8
- 4) Norman, page 218
- 5) Norman, page 241
- 6) Friedman, page 259
- 7) Friedman, page 265
- 8) Brown, page 286
- 9) Brown, page 289
- 10) Putnam and Garrett, page 2
- 11) Axelrod, page 158
- 12) Axelrod, pages 158-9
- 13) Friedman, page 283
- 14) Friedman, page 300
- 15) Friedman, page 304
- 16) Friedman, page 306
- 17) Putnam and Garrett, pages 166-7
- 18) Carter, page 487
- 19) Putnam and Garrett, page 285
- 20) Putnam and Garrett, page 285
- 21) Putnam and Garrett, page 33
- 22) Putnam and Garrett, page 35
- 23) Putnam and Garrett, page 171
- 24) Putnam and Garrett, page 80
- 25) Henderson, page 204
- 26) Sandel, page 5
- 27) Sandel, page 5
- 28) Sandel, page 5
- 29) Case and Deaton, pages 142-143
- 30) Henderson, page 8
- 31) Henderson, page 26
- 32) Henderson, page 44
- 33) Henderson, page 244
- 34) Bower, Leonard and Paine, page xx, preface
- 35) Bower, Leonard and Paine, pages 250-277
- 36) Bower, Leonard and Paine, page 237-8

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