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THE MYTH OF THE INVISIBLE HAND IN CONTEMPORARY CAPITALISM¹

Sampie Terreblanche

I am a great admirer of Adam Smith. I am in agreement with Joseph Stiglitz that “no idea has had more power than that of Adam Smith’s invisible hand”. Unfortunately, it attained this power not for the right reasons, but for the wrong ones. The ‘invisible hand’ idea has become a *myth* that is carefully and assiduously propagated by those with a vested interest in the boundless freedom and ‘space’ offered to them by unfettered capitalism. This myth is used as ideology propaganda to legitimise unbridled capitalism and free market fundamentalism. This legitimisation covers at least three serious deficiencies of contemporary and global capitalism under a thick layer of dogmatism. These deficiencies are not acknowledged to the necessary degree by the dogmatic protagonists of unfettered capitalism and also not by the academic fraternity of neo-classical economists.

These three deficiencies are firstly, the misconception that it is not necessary for business people to account themselves about the moral or ethical content of their actions because the mysterious and ‘god-like’ co-ordinating function of the ‘invisible hand’ will reconcile their selfish and greedy behaviour into a morally, agreeable end result; secondly, the misconception that the ‘invisible hand’ makes it unnecessary for society to account itself explicitly about what its common interest (or bound commune) is, or ought to be, because society can have *trust* that individuals in the pursuit of their self-interest in a competitive market system will be led – by the ‘invisible hand’ – to the general betterment of the community; and thirdly, that in a system of competitive markets – as a Smithian system is supposed to be – no individual or organisation will be *powerful* enough to disrupt the beneficial working of the ‘invisible hand’.

As long as neo-classical economists and dogmatic propagandists of capitalism continue to believe – explicitly or implicitly – in the *myth* of the ‘invisible hand’ and in its ‘god-like’ organisational capacities, it will be difficult to convince society, firstly, about the serious *ethical* problems associated with contemporary capitalism on the micro (or individual) level, on the macro (or systemic) level and on the global level; secondly, about the inability of contemporary

¹ Paper read at the 2nd International Conference on Contemporary Management (2004 ICCM Conference) at Stellenboch, South Africa on 6 September 2004.

(and global) capitalism to allocate resources efficiently enough to promote the general interest of society (or of the world population) effectively, and that the *trust* the public is supposed to have in the miraculous organisational function of a market orientated economy – in countries and globally - is not justifiable; and thirdly, about the non-competitive nature of modern capitalism mainly as a result of the spectacular rise of multi-national corporations (MNC) over the past 50 years that created huge organisations, powerful enough to be a law unto themselves and powerful enough not only to defy government regulations but also the scrutiny of public opinion and civil society.

In the rest of this paper, I will try to address the following four questions:

- (i) Is it proper for business people to use the *myth* of the ‘invisible hand’ to exonerate themselves from moral responsibility in their decision-making?
- (ii) Is it proper to have *trust* in the ability of contemporary capitalism to allocate resources efficiently and to serve the general interest of society effectively, if we are realistic about the strict conditions that ought to be in place before the ‘invisible hand’ can be operational?
- (iii) Is a contemporary capitalist system still competitive enough (as Adam Smith’s ‘invisible hand’ requires) to neutralize the power of the MNC’s and other powerful organisations?
- (iv) Is it proper to make the myth of the ‘invisible hand’ and market fundamentalism applicable on global capitalism as is done by the Bretton Woods Institutions and their dogmatic supporters?

1. THE MYTH ‘INVISIBLE HAND’ AND MORAL ISSUES IN CONTEMPORARY CAPITALISM

Many businessmen and economists like to believe that Adam Smith, with his ‘invisible hand’ doctrine, was a strong protagonist of free market fundamentalism. This is a rather vulgar interpretation of Smith’s doctrine. Smith was circumspect in his view of the ‘invisible hand’ and presumed that very strict conditions must be in place before the ‘invisible hand’ can be operational. Adam Smith was not a free marketeer, but belonged to what we can call an Institutionalise school of economics. His first condition set by him was elaborated in his *Theory of Moral Sentiments* (TMS, 1759). In it he developed a ‘model’ about how a society ought to be

organised to solve the 'Hobbes problem', i.e. the claim that human beings are not moral beings, but selfish 'beasts'.²

The popular idea that Adam Smith was of the opinion that individuals can act with ruthless individualism and can pursue their self-interest with greedy selfishness without any moral consideration or sensitivity for the interest of others, is a false interpretation of his views. This interpretation can indeed be associated with Mandeville, Hobbes and the later Social Darwinists.

In his solution of the moral problem, Smith was influenced by the 'order' Isaac Newton 'discovered' in the universe (and especially in the starry heavens). Newton regarded the universe as a perfect 'architectural design', which is so designed that the principle of gravity controlled the movement of the sun, moon, the planets and their satellites in such a way that if one of the heavenly bodies should move out of its orbit and so threaten the heavenly 'order', the 'binding links' (or disciplinary forces) would spontaneously be set in operation and would 'force' (or discipline) that heavenly body back into its proper orbit. In his imitation of Newton's 'design', Adam Smith was optimistic that society can be 'designed' in such a way that individuals will be free to move in their own 'orbits' and that 'binding links' would 'discipline' each individual to return to his/her proper orbit if he/she were to deviate from his/her orbit and behave in morally dubious (or in a socially disruptive) ways. When Adam Smith wrote his *Wealth of Nations* (WoN, 1776) he took it for granted that a 'good' society was already in place and that all individuals were already disciplined to pursue their self-interest prudently and with sensitivity for the interests of others.

² Hobbes alleged that there exists "a general inclination of all mankind, a perpetual desire of Power after Power, that ceaseth only in Death" (*Leviathan*, 1651).

In his two recent books the Nobel Prize laureate, Joseph Stiglitz, expressed serious misgivings about the ethical character of contemporary capitalism (Stiglitz, 2002 and 2003). According to him, business people are inclined to use the myth of the 'invisible hand' in an unwarranted way to justify their ruthless individualism and their immoral and anti-social behaviour. According to him the myth of the 'invisible hand' is for these businessmen a great relief. They like to believe that "it told them [that] by doing well (for themselves) they [are] doing well [for society] ... [and that they] should feel no guilt in greed, [but] should feel pride [in it]" (2003:14). These businessmen are – according to Stiglitz - of the opinion that the 'invisible hand' exonerates them from moral responsibilities. The alleged miraculous (or 'god-like') manner in which the myth of the 'invisible hand' ensures that individuals – in the pursuit of their self-interest – will unintentionally promote the general betterment of the community, creates for many businessmen a situation in which it is never necessary for them to ask what is the *right* thing to do, but only to ask what they *want* to do, what will make them rich and happy. This distorted "Smithian logic seemed to suggest that there [is] no role for morals [and] for virtues like loyalty and trust [in contemporary capitalism]" (2003:108-9). By interpreting this myth of the 'invisible hand' in this skewed manner, business people like to believe that they act morally when they increase their profits and when they are obedient to the relentless discipline of the 'bottom line'. This 'obsession with the bottom line', put pressure ... [on] firms that might have believed in honest accounting ... [to partake] in the race to the bottom" (2003:174). According to Stiglitz, we have reached a point in contemporary capitalism where,

"morality in both the private and the public sector took on a new meaning: increased profits ... Unfortunately, as convenient as it would be, there is no basis for these Smithian beliefs ... The captains of industry – the leaders to whom [we] were told to look up to – have, it turns out, acted in ways which benefited themselves at the expense of others. At least in retrospect, "*their actions looked deeply immoral*" ...the problem was not just a couple of bad apples ... as time went on more and more apples seemed rotten" (Stiglitz, 2003:308-309).

Stiglitz's conclusion that business people are inclined to act immorally in their pursuit to maximise their profits, has far-reaching implications for not only contemporary capitalism, but also for mainstream economists. The neo-classical school of economics claim that economics is – and ought to be – a value-free subject and that economists must refrain themselves from any moral judgements. In the 'model world' of the neo-classical school, all market players are supposed to act rationally. Consequently, moral issues are not even considered by these economists. With this approach, the neo-classical school of economists creates an atmosphere in which business people can act without considering the moral content of their actions. They have at least two convenient excuses, firstly, that the myth of the 'invisible hand' exonerates them

from moral responsibilities, and secondly, that mainstream economists will not scrutinise the moral or immoral nature of their actions.

When an economic system is based on the amoral – or even immoral – actions of individuals on the micro-level, then we certainly cannot expect that the macro-structures of society will remain good and beneficial. If business people are indeed encouraged to feel no guilt in greediness, then it is likely that the system will in due course become permeated by greediness and selfishness. Whether contemporary capitalism has already deteriorated into a system that is deprived of moral content, is a highly controversial matter. To allege that it is already the case, will boil down to a moral condemnation of the system. This will, probably, be too harsh a judgement. At the same time, it cannot be denied that key role-players in capitalism act in morally indifferent ways and are using rather doubtful arguments to justify their behaviour. These actions undoubtedly compromise the moral integrity of the system. If we also take account of the popular excuse that the pressures inherent to the capitalist system – i.e. systemic pressures that reflect the immutable working out of economic laws – are of such nature that role-players often do not have any choice but to act in morally doubtful ways in order to be profitable (or to survive), then the suspicion about a large degree of *systemic corruption* in contemporary capitalism becomes irrefutable. Capitalism is not a ‘natural construct’ in which rigid laws are applicable as is the case in nature. Capitalism is a ‘human construct’ and therefore it is a realm in which moral considerations ought to be applicable. When key players are allowed to exonerate themselves from moral responsibility, *systemic evilness* becomes inevitably a characteristic of contemporary capitalism – especially if the unequal distribution of corporate power and the lack of democratic control over corporate power are taken into account. (See section 4 below).

It is rather a mighty irony that while Adam Smith was of the opinion that a ‘good’ society is a prerequisite for ‘good’ individuals, we in contemporary capitalism are confronted with a situation in which a ‘bad’ system is creating pressures that ‘produce’ ‘bad’ individuals, while the virtues of this ‘bad’ system is still legitimised – unwarrantedly – in the name of Adam Smith! Sixty years ago Joseph Schumpeter was already concerned about what he has called the ‘bourgeois scheme of values’ – cultivated by capitalism – and its negative influence on the moral quality of the ‘civilization of capitalism’. According to him, people in the capitalist world should “care less for the efficiency of the capitalist process in producing economic and cultural values, than for the kind of human beings that it turns out and then leaves to their own devices, free to make a mess of their lives” (Schumpeter, 1942[1950]: 129). Schumpeter was also of the opinion that capitalism will ‘produce’ over the long run a ‘civilisation’ that will not be conducive to the survival of capitalism. According to him capitalism will not collapse ‘under the weight of

economic failure, but ... its very success [will] undermine[s] the social institutions that protect it, and 'inevitably' create conditions in which it will not be able to live" (*Ibid*: 61).

Sigmund Bauman describes the present 'civilization of capitalism' as a 'consumer society' that has replaced the 'producer society' of the 19th and early 20th centuries. He describes this stage in the 'civilization of capitalism' as follows:

"In its present late-modern, second-modern and post-modern stage, [capitalist] society engages its members – *primarily* – in their capacity as *consumers*. The way present-day society *shapes* up its members is dictated first and foremost by the need to play the role of consumer ... To increase their capacity for consumption, consumers must never be given rest. They need to be constantly exposed to new temptations in order to be kept in a state of constantly seething, never wilting excitation and, indeed, in a state of suspicion and dissatisfaction ...

In a properly working consumer society consumers seek actively to be seduced. They live from attraction to attraction, from temptation to temptation, from swallowing one bait of fishing for another ... To act like that is, for the fully-fledged, mature consumer, a compulsion, a must; yet that 'must', that *internalised* pressure, that impossibility of living one's life in any other way, reveals itself to them in the form of a free exercise of will. The market ... has already picked them up and *groomed* them as consumers, and so deprived them of their freedom to ignore its temptations ...

[The outstanding characteristic] of the consumer society [is] the entrenchment of [the] consumerist culture ... Choice is the consumer society's meta-value, the value with which to evaluate and rank all other values. And no wonder, since the "choosiness" of the consumer is but a reflection of competitiveness, the life-blood of the market. To survive, and even more to thrive, the consumer market must first shape the consumer to its own image: the choice is what competition offers ... The right type of consumer is a person who cherishes the right to choose more than the object of choice ... The excitement of the new and unprecedented sensation is the name of the consumer game ... Desire does not desire satisfaction ... to the contrary, desire desires desire; the desire to be an *ideal* consumer" (Bauman, 1998: 24-26 and 58).

The consumer society 'groomed' by consumerism is a far cry from the 'good' society envisaged by Adam Smith. While he expected of a good and open society to *restrain* the selfishness of individuals, the contemporary consumer society seduced individuals deliberately towards *unrestrained* selfishness and to irrational and insatiable greediness.

Contemporary capitalism has developed into a system that demands contradictory attitudes from the entrepreneurial and the consumer classes. The discipline of the 'bottom line', forced the entrepreneurial class to act *rationally*, to ignore moral norms in its quest for profits, to be efficient and not to be responsible for any waste. The consumer class, in its turn, is deliberately seduced by consumerism to act *irrationally* and never to feel satisfied or content. In sharp

contrast with Adam Smith, the protagonists of contemporary capitalism do not take the Smithian 'good' society as their point of departure, but the all-embracing capitalist civilization with its inherent tendencies towards *systemic corruption* and *systemic evilness*. In this 'civilization' both the entrepreneurial class and the consumer class are either 'pressurised' or 'seduced' by systemic forces to act either morally indifferent or openly selfish and to take pride in the fact that they act in morally doubtful manners. It is indeed a convenient excuse to believe that in spite of these morally doubtful behaviour patterns competitive markets – i.e. the 'invisible hand' – will create an earthly heaven. It is a convenient, but a very much-misguided belief.

2. THE MYTH OF THE 'INVISIBLE HAND' AND TRUST IN THE EFFICIENCY AND EFFECTIVENESS OF CONTEMPORARY CAPITALISM

Adam Smith describes in his *Wealth of Nations* (WoN) (1937, 1776) the strict additional conditions that ought to be in place before the 'invisible hand' will lead not only to a social equilibrium, but also to an economic equilibrium, i.e. to a situation in which scarce resources will be allocated efficiently and the general interest of society will be promoted effectively. One of these conditions that should exist in all markets is that no company or group of companies should be powerful enough to defy the disciplinary working of the market mechanism. (This condition will be discussed in section 4 below). Other conditions are that property should be distributed rather evenly and that the legal system should define and protect property rights to a satisfactory degree.

Important research has been done over the past 30 years to establish the full spectrum of conditions necessary to assure that a market orientated system will indeed allocate scarce resources efficiently and will indeed promote the general interest of society at large. Three prominent economists (all three Nobel Prize laureates) have established the full spectrum of conditions that must be in place – additional to a 'good' society and competitive markets – before the invisible hand can 'deliver' efficient and effective outcomes. These three economists are Gerard Debreu, Kenneth Arrow and Joseph Stiglitz. Among the additional conditions identified by them, are a number of unrealisable conditions such as that information must be either perfect, or at least not affected by anything going on in the economy, and that whatever information anybody had, others had the same information and the market players can buy insurance against any possible risk. Although nobody can deny that these assumptions are unrealisable, there was a hope (especially in the ranks of the free market fundamentalists) that if the real world did not depart too much from the identified conditions – i.e. if information were not too imperfect, or firms did not have too much power – that Adam Smith's invisible hand

theory would still provide a good description of the way in which contemporary capitalism operates. This hope is based on blind faith – especially by those who benefited most from market fundamentalism. It is, however, a hope that has no basis in economics as a social science. The research of the economists – mentioned above – has shown that the distance between the ideal conditions and the hard reality is far too large and that the reason why the invisible hand may be invisible is that it simply is not there!⁵

Contemporary capitalism – in especially the developed world – continues to be a very powerful engine of production. Unfortunately, the high levels of production happens in odd conjunction with very serious market failures: the reckless exploitation of scarce resources, environmental pollution that endangers continued existence of life on our planet, ‘jobless’ growth, sharp inequalities in the distribution of income, opportunities and property (within countries and especially between the Rich North and the Poor South), and growing ‘dissatisfaction’ in the Rich North in spite of ‘super-abundance’ and artificial scarcity. Apart from these ‘market failures’ contemporary capitalism also suffers from a plethora of ‘legal failures’: property rights are very unequally distributed, often difficult to define and to protect, contracts are often ambiguous, while litigation is extremely expensive. As a result of all these deficiencies many role players – and especially the executive of large corporations – are succeeding in pursuing their own interests in spectacularly successful ways for themselves, but without strengthening the economy. As they benefit, others pay the price. This situation brings Stiglitz to the conclusion that “hidden theft had evidently been part of capitalism for a long time” (Stiglitz, 2003: 173).

A very important ingredient of an economic system is the public’s *trust*. What makes economic systems work, over the long run, is trust? Lack of trust has been an important – if not the most important – reason for the disastrous breakdown of other economic systems in history. The public continues to maintain trust in a system as long as it ‘delivers’ in practice - to a satisfactory degree - what is promised in theory. Whether contemporary capitalism is still *trustworthy* is a highly controversial question. Let us consider the ‘trust’ issue only in developed countries⁶. If we take cognisance of the doubtful ways in which role players exonerate themselves from moral

⁵ Adam Smith was realistic enough to realise the conditions necessary for the ‘invisible hand’ to be operational, are unattainable. He wrote: “To expect, indeed, that the freedom of trade should ever be entirely restored in Great Britain, is as absurd that an Oceana or Utopia should ever be established in it. Not only prejudices of the public, but what is much more unconquerable, the private interest of many individuals, irresistible oppose it” (Smith, 1776 [1937]: 437-8).

⁶ In the developing countries there exist more convincing reasons why capitalism can not be trusted. In almost all developing countries a considerable part of the population – from 30% to 50% of the total population – is *systemically excluded* from the mainstream (or the capitalist sector) of the economy. In these countries the poorest 30% to 50% of the population is trapped in a situation of structural unemployment, structural inequality and structural poverty or misery.

responsibilities, of the deceptive nature of consumerism, of all the market and legal failures of capitalism, of growing unemployment, inequality, poverty and social exclusion, then we can make a strong case that contemporary capitalism is not to a satisfactory degree worthy of the trust people still display in it. This brings us to a very important question. Why are the public maintaining its trust in it, if it is true that its *trustworthiness* has become highly questionable?

This apparent contradiction can be attributed to the effective manner in which the protagonists of free market fundamentalism are using the myth of the 'invisible hand' and the ideology of consumerism to give ideological legitimation to contemporary capitalism – a legitimation that it does not deserve. But how long can the ideological and propagandistic varnish conceal the structural cracks in the edifice of contemporary capitalism? The answer to this question depends on how the 'power issue' is going to play itself out, i.e. how the contradictions and tensions created by unequal power constellations (economic, political and ideological power constellations) *within* the developed countries and *between* the Rich North and the Poor South are going to be resolved, say, within the next decade or two. Manuel Castells is of the opinion that if the logic of informationalism (as he described mass ideological propaganda with the help of the new mass media) and the logic of globalisation is taken into account, then it seems unlikely that the structural cracks in the edifice of contemporary capitalism will be uncovered (Castells, 2004: Ch 2). The structural power to the disposal of the capitalist class – and especially at the disposal of global corporatism – is so overwhelmingly strong and so well-integrated, that it can in all probability squash whatever resistance can be put up against it – at least for a considerable period of time. In the next section the 'power game' within developed countries and between the Rich North and the Poor South (within the framework of global capitalism) will be discussed.

3. THE MYTH OF THE 'INVISIBLE HAND' AND UNCONTROLLED ORGANISATIONAL POWER

Adam Smith was in his *WoN* (1776) primarily concerned with the problems that arose due to the already outdated mercantile system. He was particularly opposed to the way in which commercial companies – like the British East Indian Company – abused their charters (granted to them by the British Government some 200 years earlier) to the companies particular advantage, but to the detriment of the *general interest* of society as a whole. In his zeal to break the monopolies of the merchant monopolists, Adam Smith fervently advocated a market system with a high level of competition between large numbers of small competitors. If the competitive condition - together with all the other conditions set by him - were in place, individuals pursuing their self interest will – according to him – be led by the 'invisible hand' to promote the general interest of society at large. If these conditions were not in place, then the 'invisible hand' will, of course, not be there.

Smith was deeply opposed to joint-stock companies, now called corporations. According to him "people of the same trade seldom meet together ... but the conversation ends in the conspiracy against the public" (Smith, 1776 [1937]: 28). He was even more strongly opposed to corporations with monopolistic power and to corporations powerful enough to defy the discipline of the market. Strangely enough, it is today mainly the big and multi-national corporations that are the champions of the myth of the 'invisible hand'. The vested interest of big business interest in the 'invisible hand' is not based on its efficiency and effectiveness, but on the 'freedom' and the 'space' its mythical existence creates for business to do as they like.

Kenneth Galbraith has expressed the wish that Adam Smith be invited to address a joint meeting of say the 30 000 MNC's in America. According to Galbraith, Smith would be astonished to hear the heads of great corporations – or greater conglomerates or combines - proclaiming their economic virtue in his name. They, in their turn, would be appalled when he – of all prophets – told them their enterprises should not exist (Galbraith, 1977: 27).

It is rather strange that in the 'ideal' economic cosmology envisaged by Adam Smith, no provision was made for the existence of large and powerful organisations like MNC's, like trade-unions, like non-governmental organisations, pressure groups, etc. The rise of large corporations and large organisations with large and cumbersome bureaucracies and with tyrannical power at their disposal, is mainly a phenomenon of the 20th century. Parallel with the rise of large organisational structures during the 20th century, we also experienced the rise of the mass media

and the rise of massive ideological propaganda – with the help of the mass media – to legitimise the power and influence of these organisational structures. According to Kenneth Galbraith the power of the managerial elite of the MNC's depends on their ability to create for themselves a more attractive (or more acceptable) image - through ideological propaganda – than what the true reality is:

“The institution that most changes our lives we least understand, or more correctly, seek most elaborately to misunderstand. That is the modern corporation. Week by week, month by month, year by year, it exercises a greater influence on our livelihood and the way we live than unions, universities, politicians, and the government. There is a corporate *myth*, which is carefully, assiduously propagated. And there is the *reality*. They bear little relation to each other. The modern corporation lives in suspension between fiction and truth” (Galbraith, 1977: 257).

This is also true of large organisations. There is an organisational *myth*, and there is an organisational *reality*. They bear little relation to each other. It is important to realise that we are living in a period of ideological propaganda *par excellence*. The propaganda of our period can only be matched by the ‘ideological’ propaganda of the Roman Catholic Church in the medieval period.

The rise of multi-national corporations and large national and international organisations was the inevitable result of huge advancement in production, organisational and communication technologies during the 20th century. While the rise of large corporations and large organisations dramatically increased the ‘output’ of goods and services and brought about an astonishing global inter-connectedness, the power concentrated in the hands of these organisations’ create all kinds of tension and contradictions in and between contemporary democracy and contemporary capitalism. Many of the organisational structures are powerful enough to challenge and even defy the prescripts of democratically elected governments. The chief executive officers (CEO's) of the big organisations can often not be held accountable for the way in which they exercise their power. This is a serious matter. We are living in a supposedly democratic era. The fundamental idea of democracy is that *all* forms of power – whether economic, political or ideological power – must continuously be open for scrutiny by public opinion - either directly or indirectly by civil organisations or by parliament or by legal prescripts⁷.

⁷ The distinction made by Susan Strange between *relational* and *structural* power is relevant for an understanding of the way in which the ‘power game’ is played. Relational power is the power that one actor wields directly against other player(s). Structural power, however, is the ability of an actor (or group of actors) to shape the rules that other actors (the state and civil society) follow, thus enabling that first actor(s) to insidiously achieve its objectives without any confrontation, since the other actor accept the new rules as norms and do not realise the true basis of structural power until later (see Strange, 1994 and 1996).

Corporations and organisations are obliged to hold annual meetings with shareholders or with members and are also obliged to let their books be audited annually. But the control function of annual meetings and the auditing process have become very much watered down through manipulations in the organisational 'power games'. Consequently, many large organisations are powerful enough to promote their – or their executives' - interest to the detriment of society. The best example of this, is the bankruptcy of Enron and Arthur Anderson. These events demonstrate the extent to which contemporary capitalism has become 'hallowed' by uncontrolled power. We can talk about the 'unionization' of corporative capitalism. The damage done by the 'unionization' process is probably much larger and more widespread than is generally realised or acknowledged. When the power – or more specifically the *uncontrolled* power – of large organisations and their abundant opportunities to be involved in 'hidden theft', are taken into account, then all the talk about the co-ordinating function of the 'invisible hand' becomes not only ludicrous and outrageous, but even dangerous.

During the third quarter of the 20th century the theory of pluralism was elaborated. According to this theory it was claimed that power is distributed in such a way between the large numbers of organisations in the modern system of democratic capitalism that a remarkable 'competitive equilibrium' is created between the large numbers of power blocks. One of the strongest protagonists of pluralism was the American political philosopher Robert Dahl. In several of his books – published between 1956 and 1980 – he propagated the idea that power is effectively disaggregated and non-cumulative and that it is shared and bartered by a network of numerous groups in society representing diverse interests. However, in a book published in 1985 he radically changed his point of view, concluding that "modern corporate capitalism tends to produce inequalities in social and economic resources [and power] so great as to bring about severe violations of political equality and hence of the democratic process". According to this neo-pluralist view of Dahl and others, interest groups (such as the big corporations) cannot be treated as necessarily equal, and the state cannot be regarded as a neutral arbiter among all interest groups. According to the neo-pluralist view, the big business corporations wield disproportionate influence over the state, and therefore become a threat to both capitalism and democracy and jeopardise the ability of governments to govern effectively (see Dahl, 1985: 60).

4. THE MYTH OF THE 'INVISIBLE HAND' AND GLOBAL CAPITALISM

The rise of global capitalism over the past 30 years is closely connected with the 'rediscovery' - at the end of the 1970s - of the ideology of market fundamentalism. During the period of *Laissez-faire* capitalism - that stretched from 1870 to 1914 - the dominant ideology in the Western world was the ideology of market fundamentalism. This period coincided with the Pax Britannica when the world experienced what we can call global capitalism Mark 1. It was a period when the doctrines of the neoclassical school of economics were accepted uncritically. The dogmatic belief was that the market mechanism - or the 'invisible hand' - will establish equilibrium in every market and that the economy as a whole will be in 'general equilibrium' to the benefit of all. In spite of the optimistic belief in the market mechanism, the *Laissez-faire* system became permeated with irresolvable contradictions. Income was very unequally distributed and poverty was very severe. According to Keynes "there was no means open [in the *Laissez-faire* system] to a government whereby to mitigate economic distress at home except through the competitive struggle for markets" (Keynes, 1936: 382). This struggle for markets and colonies led to the First World War and ultimately to the Great Depression.

The period from 1914 until 1945 was a painful crisis period of adaptation when the Western world tried to find a new institutional and a new ideological approach to solve the serious matrix of social and economic problems. After the Second World War most of these problems were mitigated considerably by the acceptance of the Keynesian *social democratic* approach. According to this approach, the dogmatic reliance on the market was replaced by much greater government involvement in the economy and by the rise of the welfare state. It was then acknowledged that we cannot trust the 'invisible hand' to promote the general interest (or bound commune), that the state has the task to intervene and to guide production and spending patterns in directions that will indeed be conducive for the realisation of the general interest and that the general interest cannot be defined by market forces but only via the democratic process.

From 1950 until 1973 the industrialised countries experienced their Golden Age of high growth, price and exchange rate stability, full employment and a comprehensive equalisation in the distribution of income. Larger state intervention and redistribution implied that a considerable *powershift* had taken place during the transitional period (1914-1945). In the *Laissez-faire* period the business or capitalist class was in a powerful position vis-à-vis the working class. During that period the 'invisible hand' was in reality an 'iron fist' that enabled the capitalist class to enrich itself by exploiting the working class. During the Golden Age - when the social democratic

approach was implemented - the 'soft hand' of the caring social democratic approach replaced the 'iron fist' of the *Laissez-faire* period.

The Golden Age came abruptly to an end with the Egypt-Israel War (1973), with the launching of OPEC and with the sharp increase in the price of oil. The stagflation of the 1970s and the increased taxation (to pay the increasingly higher levels of unemployment insurance) created an opportunity for the corporate sectors (in mainly the USA and the UK) to "recapture" a large part of the bargaining power that has shifted since the interwar period to the working class and to the democratically elected governments. At the end of the 1970s, the managerial elite of the corporate sector succeeded with an ideological *coup d'état* by 'rediscovering' the marked fundamentalism of the *Laissez-faire* period. Pres. Reagan and Mrs Thatcher supported the corporate sector in this *coup d'état*. They implemented neo-liberal policies and deregulated financial markets. The end result of this *coup d'état* was the rise of global capitalism Mark II within the framework of the *Pax Americana*. In the present version of global capitalism the structural power of global corporation is more deeply entrenched than in any other period in history.

The worldwide spread of American MNC's during the Cold War period and the relentless competition in global markets – in conditions manipulated by successive American administrations – enabled the corporate sector to regain from 1980 onwards its power over the working class, over the welfare state and over democratic governments. The powershift in favour of global corporatism was in its turn responsible for a distributional shift towards the rich in developed countries and towards the Rich North in the 'global village'. While income became much more equally distributed from 1950 until 1980, the opposite happened since then – especially in the USA⁸. The neo-liberal school succeeded in their plea that the state should be 'rolled back' and that the welfare state should be retrenched. The 'soft hand' of the social democratic approach was again replaced by the 'global iron fist' of global markets and global corporatism.

From the mid-1970s onwards the governments of the Rich North created conditions conducive for the rise of global capitalism and global corporatism. This enabled the corporate sector in the Rich North (and especially in the United States) to change the rules of the 'global capitalist

⁸ According to Lester Thurow, the per capita income in the United States in 2000 was more than double that in 1950. But despite this huge increase in total income, the wages and salaries of the lower 60 to 70 per cent of the workforce were the same in real terms as in 1950. Between 1977 and 1999 the top fifth of households in the United States increased their annual income after federal taxes by 43 per cent, while the middle fifth gained 8 per cent, and the bottom fifth lost 9 per cent. This growing inequality brought Thurow to ask the following question: "How far can inequality rise before the system cracks?" (Thurow, 1996: 2 and 18-24).

game' to its own advantage with the assistance of the IMF, the World Bank, and other international organisations and instruments. By entrenching its own structural power, the corporate sector is continuously rewriting the rules of the 'capitalist game' within countries and also between the Rich North and Poor South. By consolidating their own structural power, the corporate sectors in all countries – but especially those in the Rich North – are tending towards usurping the powers as well as the functions of democratically elected governments. Noreena Hertz describes this phenomenon in her book, *The silent takeover: global capitalism and the death of democracy* (2001). According to her, the managerial elite of the multinational corporations is continuously increasing its power at the expense of the sovereignty of democratically elected nation states and at the expense of the lower 60% of the population in advanced capitalist countries. Manuel Castells called the new period of global capitalism the Information Age. According to him "new technological and organizational conditions of the Information Age ... provide a new, powerful twist to the old pattern of profit-seeking taking over soul-searching" (2004: 68).

The dogmatic protagonists of market fundamentalism and unrestrained globalisation include the Bretton Wood Institutions (BWIs), global corporatism, international financial institutions (IFI) as the senior partners, and the governments of the developed countries as the junior partners. The tripartite power block (between the BWI's, global corporatism and IMI's) wield such power in the structure of global capitalism that the Poor South is in effect being recolonised. This power block based its ideological approach on the view that the Smithian 'invisible hand' has (again) become operational with the 'opening' of global markets and with the 'free' flow of capital and trade and that the advantages of 'globalisation' will in due time spread to every corner of the globe.

It cannot be denied that global capitalism has many advantages. Unfortunately, the advantages are mainly restricted to the Rich North, while the disadvantages are 'shifted' mainly on the Poor South. In 1970 18% of the world's population lived in the Rich North and received 70% of global income. Since then the world experienced the spectacular rise of global capitalism. The population of the Rich North is now 15% of the population of the world, but its share of global income has increased to 80% of global income. The population of the Poor South increased from 82% of the world's population in 1970 to 85% today, but their share of total income declined from 30% to 20% of global income. Almost 50% of the world's population (i.e. 2,8 billion persons) live on less than R2 a day. In China and some other Asian countries income has increased. In the poorest 50 countries – mostly in Africa – income has declined rather sharply over the past 30 years. The share of the Poor South in foreign direct investment (FDI) has

increased only from 18% of the total flow (if we exclude China) in 1983 to 21% in 1994 (Chang, 2003: 251). Most countries in the Poor South receive FDI equal to only 1% of their GDP. According to *The Economist* (3 May, 2003) it is unlikely that FDI flow to the Poor South will increase.

5. CONCLUSION ON THE APPLICABILITY OF THE 'INVISIBLE HAND' IN GLOBAL CAPITALISM

In sections 2, 3 and 4 we discussed the strict conditions that ought to be in place before the 'invisible hand' can be operational. We come to the conclusion that the dogmatic belief in market fundamentalism in developed countries is unjustifiable. Astonishingly enough, the 'model' of market fundamentalism has also been made applicable on global capitalism over the past 25 years in spite of the fact that the hard reality in the 'global village' militates even more strongly against this 'model'. The main characteristics of global capitalism can be summarised as follows:

- (a) While enormous power – political, economical and ideological power – is concentrated in the hands of the Rich North, the Poor South is pathetically powerless. The situation of deeply entrenched structural power in the Rich North enables corporate capitalism to exploit the Poor South at ease. The 'hidden theft' that is taking place within the structures of global capitalism is probably as high – if not higher – than the colonial plunder that took place at the high point of Western imperialism.
- (b) If we take all the imperfections – of a social, legal and economic nature - in the 'global market' into account, then it is indeed presumptuous to claim – as is done by the global market fundamentalists – that a 'global invisible hand' is operational in the 'global village'. This presumed 'global invisible hand' can simply not be a 'godlike' or a benevolent 'hand', but can only be a cruel 'global iron fist'. This presumed 'global invisible hand' is for the global entrepreneurs a great relief. In believing in the benevolence of the presumed 'global invisible hand', the global entrepreneurs are seemingly convinced that by doing well for themselves, they are doing well for the global population. They feel no guilt in global greed, but only pride in it, because they like to believe that they are serving humanity at large!
- (c) It is from a moral point of view completely unacceptable that 15% of the world's population receive 80% of income, while 85% receive only 20%. If the power structures in place in global capitalism should be perpetuated until 2040, it is quite possible that $\pm 10\%$ of the world's population will then receive $\pm 90\%$ of global income!

- (d) The moral amenability of the unequal income and the unequal consumption patterns between the Rich North and Poor South becomes so much more untenable – and even morally despicable - if consumerism is taken into account. While one billion people are seduced by consumerism to desire and to satisfy artificially created needs of the most fatuous (vacuous) nature, three billion people in the Poor South are also exposed to some of the seductions of consumerism, but they are structurally deprived of opportunities to satisfy their basic human needs. We are indeed living in a cruel ‘global village’.
- (e) While the Rich North ‘produced’ almost 80% of the world product, it is responsible for more than 70% of the pollution and the exploitation of non-renewable resources. Although the large populations of China and India also create environmental problems, a child born in the USA will cause in his lifespan of 70 years forty times more ‘harm’ to the environment than a child born in India and also lives for 70 years.
- (f) In spite of the claim of the dogmatic protagonists of global capitalism that all global markets are ‘open’ – or will be ‘open’ shortly – this is simply not the case. Stiglitz accused the developed countries of “*hypocrisy* by pretending to help developed countries by *forcing* them to open up their markets to the goods of the advanced industrial countries while keeping their own markets protected” (Stiglitz, 2002: xv).
- (g) The Bretton Woods Institutions are highly unrealistic in their dogmatic application of the Washington Consensus policies in the Poor South. When applying their ‘structural adjustment programmes’ they take it for granted that the developing countries do have the institutional framework necessary to be regarded as capitalist countries. This is simply not the case – especially not in large parts of Africa. In these countries property rights are ill-developed and very unequally spread, a legal system to define and protect property rights is often non-existent, while communication networks are unreliable and the majority of the people are not rational and/or materialistically orientated, but uneducated and to a large degree still traditionalist and feudally orientated. Most of the countries in Africa South of the Sahara (ASS) do not experience the recognised market failure, but the phenomenon of *market failure*, i.e. the market system *per se* fails because it is by far not properly institutionalised. Unfortunately the BWIs – blinded by their market fundamentalism – are apparently unaware of this market failure. Consequently, their ‘structural adjustment programmes’ have caused immeasurable harm in the Poor South and especially in ASS.

- (h) Global capitalism is a highly undemocratic system⁹. While the politico-economic system in developed countries is a system of *democratic* capitalism, global capitalism is not at all complemented by a system of global *democracy*. In developed countries the political system of democracy and the economic system of capitalism have become closely intertwined: they operate in many ways interdependently, the one compensates for 'failures' of the other and the one constrains the power of the other. In spite of this 'intertwined' relationship, the corporate sector is increasingly dominating the democratically elected governments in developed countries over the last 25 years. In the 'global village' the situation is much worse. The 'global village' has become the 'playing field' of global corporatism, but in this 'village' there is no 'global government' to hold global corporatism accountable for the way in which it exercises its global power. The political organisations that operate in the global arena – like the Security Council of the UN and the G7 – are dominated by the Rich North and promote the interest of the developed countries. The political powerlessness of the Poor South in the global arena has far reaching implications for countries in the Poor South. It creates 'space' for big corporations and big organisations (like the IMF) to misuse their power in countries in the Poor South without being called to account themselves about the doubtful way in which they are exercising their power. The 'enronization' of global capitalism happens on a much larger scale than what is the case in developed countries¹⁰.

I am in agreement with John Sitton's evaluation of contemporary capitalism:

"For all of its bravado, contemporary capitalism is at an *impasse*. It continues to form powerful forces of production yet is apparently incapable of applying these forces so as to satisfy basic needs of the world's population. There is economic growth, but also mass poverty and environmental destruction. Even in the developed world, productivity grows in odd conjunction with a determined attack on standards of living and entitlements, mass unemployment and a vicious scapegoating to explain the general experience of decline" (Sitton, 2003: xi)

⁹ Stiglitz puts it as follows: "The problem is that economic globalization has outpaced political globalization. The United States has been successful in selling the idea of democracy around the world ... But in the global arena, the United States has repeatedly made it clear that it must get its way. If it can do so through using whatever power it has including its economic power, all the better; if it cannot, it will go its own way ... Globalization has meant that the countries of the world are more closely integrated, and with closer integration inevitably comes a greater need for *collective* action, to solve *common* problems ... Yet America has been reluctant to accept that [collective] decisions that effect the whole world ought to be made in a way which is consonant with democratic principles" (Stiglitz, 2003: 313).

¹⁰ Due to the rise of transnational corporations and other so-called 'transnational actors' we experience a growing interest in the notions of these international institutions as moral agents. (See Erskine (Ed.), 2003).

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Possible question(s)

Write an essay on Adam Smith's Invisible Hand, on how it became a myth and on the misuse that is made of this myth.