

UNIVERSITA' DEGLI STUDI DI NAPOLI FEDERICO II

DOTTORATO DI RICERCA IN SCIENZE ECONOMICHE

XVIII CICLO

**THORSTEIN VEBLEN ON INCOME DISTRIBUTION,
INSTITUTIONAL CHANGE AND ECONOMIC DEVELOPMENT**

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INTRODUCTION

The writings of Thorstein Veblen (1857-1929) – American economist, teaching fellow at the University of Chicago, Stanford, Missouri, and at the New York School of Social Research and editor of the *Journal of Political Economy* – have recently enjoyed a renewed interest. It will be sufficient to recall that in 1998 the *Cambridge Journal of Economics* devoted a special issue to Veblen's economics and that in 2003 – thanks to Rick Tilman – about ninety essays on Veblen's whole thought were collected. As regards his contribution to economics, scholars have mainly focused their attention on his methodology and on his theory of institutional changes. Less emphasis has been placed on his analysis of the determinants of unemployment and income distribution.

The aim of this work is to provide a re-reading of Veblen's economics with particular regard to these latter issues. In particular, the following main questions are in order: *a)* What are the main causes of unemployment according to Veblen's works? *b)* How can the dynamics of income distribution affect economic growth and institutional changes?

On the methodological plane this is a work of *history of economic analysis*, in accordance to the method suggested, amongst others, by Takashi Negishi who writes in his *History of Economic Theory*: “we hope we can find in the works of past economists clues to questions of present interest or theories and techniques of analysis that might be applied to modern problems”, while also accepting the vision of a “competitive” development of economic ideas as pointed out by Alessandro Roncaglia in his *La Ricchezza delle Idee* (2001).

This book explores the idea that Veblen's theoretical framework is based on the assumption that contemporary economies are credit economies and conflictual economies. Credit – managed, as will be shown, by the leisure class – is conceived as a means of capitalization, thus of expansion of firms aimed at monopolistic control of markets. Conflict involves two dimensions: *a)* on the microeconomic plane, that is to say within the firm, where undertakers and technicians have contrasting targets for the level of production (‘internal conflict’); *b)* on the macroeconomic plane, that is to say, within the social-political arena, where the behaviour of members of the leisure class –

aimed at consuming for the purpose of ostentation and competition – *can* produce waste to the detriment of the underlying population (‘external conflict’).

It will be argued that unemployment ultimately depends on the existence both of internal and external conflicts, due to the following mechanisms. In a context of conflictual economy the firm becomes a *locus* of conflict between undertakers and technicians. undertakers want to reduce production in order to maintain high prices and obtain high monetary profits, while technicians want to maintain a high production since production is the concrete form in which they show their skill, efficiency and knowledge. The internal conflict therefore derives from the “clash” between two tendentially incompatible instincts: the *workmanship* of technicians and the *predation* of undertakers. When *predation* defeats *workmanship*, unemployment occurs. In fact employment is a function of the degree of utilization of capital, which is reduced if the undertakers’ profit aim overcomes the technicians’ production aim. This kind of unemployment can be called *unemployment from internal conflict or from under utilization of capital*. When the degree of capital utilization falls, both prices and profits increase; the increase in prices determines a reduction of real wages. The consequence is that the increase in the profit/wages ratio determines unemployment. Moreover, given the context of credit economy managed by the leisure class, the financial rent represents the main form of income for the leisure class. In particular the financial rent is assured *via* banking loans of by the acquisition of stocks and bonds. leisure class is considered here to be the class able to control the banking system and the financial market. Consequently it controls the interest rate in the monetary market and the quantity of stocks and bonds in the financial market. When the leisure class increases the level of its consumption – waste – the financial rent increases via the increase in the interest rate and the volume of stocks and bonds bought. This can generate two effects: *a)* when the financial rent increases, the leisure class increases demand for goods; this in turns generates increased investments, production and employment (*Malthusian element of Veblen*); *b)* at the same time financial rent is a financing cost for firms and when full employment is reached, there is an additional increase of rent, reduced profits, increased prices, reduced real wages. The reduction of profits combined with the reduction of the real wage determines a reduction in investment, production and employment; investments in fact are negatively affected by the high costs of financing and by the negative expectations on sales; expectations

decline since the reduction of real wages determines a reduction of demand. In both cases the increase of the rents/wages ratio has produced a reduction of investment and therefore a reduction of production and employment. This kind of unemployment can be called *unemployment from external conflict*, since it derives from the conflict in the distribution of income between social classes.

The most important result is the following: the more unequal income distribution *can be* – both in terms of the profits/wages and the rents/wages ratio - the higher is the resulting unemployment level. Note also that, in Veblen's view, income distribution does not reflect the marginal productivity of the inputs, but it originates in habits of thought.

The rereading proposed here also suggests the idea that institutional change is mainly driven by the dynamics of income distribution. The key variable is assumed to be the limit of tolerance of workers and of the unemployed. The limit of tolerance for workers and unemployed is measurable as the maximum difference tolerated between the real wage received the maximum unemployment benefit received. Note that the limit of tolerance of workers and unemployed has the same origin. In fact the state of social discontent is a consequence of policies of reduction of production; the reduction of production not only determines an increase in unemployment but also in prices, which affects the workers' real wage level. Both the workers and the unemployed can therefore feel the effects of the state of income distribution of the leisure class and when the limit is reached, social conflict occurs. When the "limit of tolerance" is reached a problem arises: How can the conflict have originated? There are two possibilities: *a)* the conflict originated from economic motives, in other words on rational grounds, or *b)* the conflict originated from moral motives, in other words on irrational grounds. In Veblen the conflict does not have an economic basis but a moral one and this is due to one main consideration: the economic grounds of the conflict call for a rational calculus on the expected benefits and costs of conflict which the Veblenian agent in fact is not able to do since s/he has no information on benefits and s/he is not rational. Being non rational, Veblen looks at morality as the main basis on which workers and the unemployed enter into conflict. The violation of the limit of tolerance – as will be argued – is the basic determinant of social conflict driven by morals. Social conflict, in turn, affects the habits of thought of the underlying population, in the sense that – via social conflict - they internalise critical attitudes

towards the existing social order and perceive waste as a non value (and, by contrast, efficiency as a value). Moreover, the social conflict determines institutional change but also economic growth. In fact social conflict pushes the system to distribute income more equally. In other words social conflict determines an increase of real wages; when real wages increase, total demand increases and undertakers are more inclined to increase the grade of utilization of capital by employing more workers.

Furnishing a clear and precise interpretation of Veblen's thought on the above topics is certainly not simple; the interpretative literature on the author knows this difficulty only too well. His peculiar writing style (ironic, satiric, literary) and his recurring polemical attitude make his writing interesting but often difficult to organize with the aim of furnishing a clear reconstruction of his thought and/or for the purpose of finding the internal consistency of his theories. As a consequence the topics presented in this work have been analysed through a preliminary study of Veblen's thought in all its complexity, then in the attempt to order it following a logic that is functional to the rationalization of the topics of the present work. In particular the analysis of the Veblenian theory of unemployment requires a preliminary critical reconstruction of the features of social classes, their instincts and habits of thought, their order within a hypothetical Veblenian macroeconomic schema in which credit and social conflict structure the productive and distributive order. Moreover the analysis of the relation between income distribution and economic growth requires a preliminary critical reconstruction of economic categories of income, their features and their attribution to each social class. Finally the relationship between the distribution dynamic, institutional change and economic growth requires a preliminary reconstruction of Veblen's theory of institutional change.

Outline of the thesis

The present work is organized as follows. Chapter one opens with the presentation of Veblen's methodology and continues with the construction of the Veblenian macroeconomic system *via* description of the social order - formed by the leisure class, undertakers, technicians and the underlying population - of the theory of instincts and institutions and their attribution to social classes. These are the steps needed to get to the presentation of the Veblenian theory of unemployment from

internal conflict. Chapter two firstly presents a description of the circuit of income production within a credit economy and then a critical description of the economic categories of income (rents, profits and wages), their features and attribution to social classes. Particular emphasis will be given to the consumption of the leisure class, to the capital of undertakers and to the institutional base of the subsistence wage since social classes in fact make reference to these objects for quantifying their income and also for structuring their actions in order to maintain effective income in line with desired income. The description of economic categories of income and their distribution between social classes is followed by the description of the second topic of the present work: that is to say economic growth and the relationship between income distribution, economic growth and employment/unemployment from external conflict. Finally, Chapter Three firstly presents a reconstruction of the Veblenian theory of institutional change emphasising his historical description of the evolution of institutions and his ideas of the role of technicians and workers as regards the process of institutional changes. After the necessary presentation of the Veblenian theory of institutional change, an expansion of his ideas is presented and the relationship between the distribution dynamic and institutional dynamic will be shown.

Acknowledgements

I am extremely grateful to Professor Guglielmo Forges Davanzati for the time and care he took in helping me during my research, Professor Giuseppe Fontana for the time and care he took in helping me during my study in Leeds, Professor Carlo Panico for his useful comments on my dealing with the Veblenian theory of prices, Professor Alfredo Del Monte for his useful comments and suggestions on organization of my work, Elena Maria Fabrizio for her precious help on my dealing with the contemporary ethics of conflict. Joan McMullin put in considerable effort into improving my English.

The usual disclaimers apply.

Andrea Pacella
November 2006

Chapter I

THE ECONOMICS OF THORSTEIN VEBLEN: INSTINCTS, INSTITUTIONAL CONFLICTS AND SOCIAL ORDER

1.1 The economics of Thorstein Veblen: some methodological issues

Thorstein Veblen's contributions to economics are different and affect different planes. In fact he was interested in numerous economic phenomena: the motivations of economic behaviour, consumption, production, distribution, growth, development and the cycle, and his way of looking at such topics was unique, not only in the original theories he put forward but also in the starting point from which he tried to explain economic matters¹. Veblen was an innovative economist first of all in his methodological approach to economics and then in his theories² and as Sweezy (1957, p.112) writes: “[scholars of modern capitalism] will find more inspiration and guidance in [Veblen's studies] than in all the rest of American social science put together”. The aim of this section is therefore to describe his contribution to economics from the methodological side before investigating the peculiarities of his theories³. For

¹ Thorstein Veblen was born on 30 July 1857 on the family farm in Wisconsin from a family of Norwegian immigrants. Veblen attended the Carleton College Academy in Minnesota from 1874 to 1877 where he studied under the economist John Bates Clark; there in 1877 he obtained his B.A. and then moved to Johns Hopkins University and Yale where he obtained his Ph.D. in philosophy in 1884. Veblen went through a long period of unemployment from 1884 to 1891. It was not until 1892 that he found a job as teaching fellow at the University of Chicago, where he worked until 1904. From 1896 he was also managing editor of the *Journal of Political Economy*; however a scandal of marital infidelity made him resign from the University of Chicago and it was only in 1906 that he obtained a new job at the University of Stanford, living at Palo Alto in California. He remained there until 1909 when a new scandal forced him into a new resignation from the University of Stanford. He moved again in 1911 to the University of Missouri for a new job, then to Washington in 1917 and then in 1919 to New York where he taught at the New School for Social Research. In 1926 he came back to Palo Alto where he died on 3 August 1929 from heart disease. For additional biographic information see, amongst others, Bates (1934); Dorfman (1932a; 1934); Lerner (1948); White (1952); Dobriansky (1957); Fredrickson (1959); Vianello (1961); Del Grosso Destri (1970); Edgell (2001).

² Gruchy (1958, pp.11-12) for example stresses that Veblen contributed to the development of economic theory in different respects: *a*) on the microeconomic plane “he was one of the first to make what we now call the administered price [and] he had enough of the essentials of economics of oligopoly”, *b*) on the macroeconomic plane “Veblen develops a rudimentary form of the nation's economic accounts in which he offsets actual total national output or total supply with various consumption and investment items or components”.

³ For a reconstruction of the style of writing see Dorfman (1932b), Conroy (1968); Horowitz (1980). On the Veblen's theoretical and historical background see Dorfman (1958), Riesman (1953). For a reconstruction of Veblen's ideology see Metzger (1949), Fusfeld (1973); Cassano (2005).

this purpose, two main methodological issues will be discussed in what follows, i.e. the Veblenian conception of economics as an evolutionary science and his view of economic phenomena as cumulative and indefinable causation phenomena.

a) Economics as an evolutionary science. Veblen considers economics an evolutionary science. As the author himself remarks (Veblen, 1961 [1898c], p.77) “[economics] is a theory of a cumulative sequence of economic institutions stated in terms of the process itself”. So he sees economics as a theory on the nature, motivations, working and effects of intertemporal sequences of economic institutions, in brief, as a theory of “cultural sequence” on economic matters (Veblen, 1961 [1898c], p.77). In particular he defines economic institutions as:

“Habitual methods of carrying on the life process of the community in contact with the material environment in which it lives” (Veblen, 1975 [1899a], p.193).

Two points can be made here. According to Veblen *a)* economic matters deal with the “material means of life” (Hobson, 1937, p.140), *b)* the meaning of economic matters changes with the changing of habits⁴. So if economics is seen as a science of economic institutions then the economic phenomenon is social. As Edgell (1975, p.267) convincingly remarks, Veblen “considers economic phenomena as a social phenomena and consequently [he recognizes] that each type of economic system presupposes a specific form of society”. In these terms, the economic phenomenon becomes a matter of social order, in other words of the peculiar structure and distribution of classes in the society. In addition, when he studies the economic phenomenon he uses a particular methodology known as *cumulative causation approach* (see, among others, Ginger, 1952; Argyrous and Sethi, 1996; Cutrona, 2003). Following this approach Veblen considers each economic phenomenon as a phenomenon whose current features are outcomes of the chain of institutions which move by a continuous shifting of past and current actions and opposing actions. In these terms the investigation of the direction of a given economic phenomenon and of its origin become the main aspects on which Veblen concentrates. Moreover he builds his economic theory on the basis of

⁴ However it is important to notice - although the intention of the present work is to investigate Veblen’s study of economic behaviour and others’ commentary on it - that “[Veblen] always treated behaviour as a whole, not caring to mark off a narrow segment as strictly economic” (Mitchell, 1973 [1929], p.605).

two particular critiques of the neoclassical approach: *a)* the critique of its ‘taxonomic’ function and *b)* the critique of its philosophical source: “natural law”.

a₁) The taxonomic issue. Veblen criticises the neoclassical approach defining it as a “taxonomic science” (Veblen 1961 [1899c], p.82; see also Veblen, 1961 [1899d], 1961 [1900]) that is to say as “essentially classificatory” theory (Edgell and Tilman, 1989, p.1005; see also Tilman, 2003, p.xix). Veblen therefore opposes the traditional cataloguing of socio-economic variables – rents, interest, profits and wages – in terms of “fixed logical relations” (Davis, 1945, p.138) since - as clarified by Davis (1945, p.138; italics added) - “[when he] defined social reality as a process continually changing [...] he implicitly reasoned that no genuine science could be founded on an assumption of fixed logical relations. No facts can legitimately be classified in *permanent abstract categories* because the facts are changing all the time”. When Davis stresses that “no facts can [...] be classified in permanent abstract categories” he is discussing another important aspect of Veblenian criticisms of neoclassical economics: The invalidity of natural law.

a₂) The rejection of the natural law view. A taxonomic science needs “immutable premises” on which it defines its features (Veblen, 1961 [1909a], p.236). Veblen argues that neoclassical economics makes reference to two particular “immutable conditions”: *a)* ownership and *b)* free contract which are assumed as given in the logic of natural rights. On this point Veblen remarks:

“The order of nature [- natural rights-] is an order of things in which men [are] conceived to be effectually equal in all those respects that are of any decided consequence - in intelligence, working capacity, initiative, opportunity, and personal worth” (Veblen, 1964 [1919a], p.36).

Being natural rights “they are part of nature of things” and consequently “there is no need of accounting for them or inquiring into them” (Veblen, 1961 [1909a], p.236). So neoclassical economics – in Veblen’s vision – seems to attribute a sort of spirituality to nature (“animism”) whose ‘behaviour’ is not casual but has a design. Natural variables are taken as exogenous that is to say they are assumed as typical, normal and definitive for each individual (see Veblen, 1961 [1909a], p.236). An economics working on this line of thought is seen by Veblen as a “pre-Darwinian economics” (see Edgell, 2001, p.68) based on – according to Coats (1954, p.529)

“outmoded preconceptions” (Coats, 1954, p.531) – which must be rejected since it is a non-evolutionary science. As Veblen remarks:

“To the pre-Darwinian [scientists] the centre of interest and attention [...] was the body of natural laws governing phenomena under the rule of causation. These natural laws were of the nature of rules of the game of causation. They formulated the immutable relations in which things ‘naturally’ stood to one another before causal disturbance took place between them, in orderly unfolding of the complement of causes involved in the transition of the interval of transient activity, and the settled relations that would supervene when the disturbance had passed and the transition from cause to effect had been consumed, - the emphasis falling on the consummation” (Veblen, 1961, [1909], p.37).

On the other hand Veblen views economics in evolutionary terms, or rather as “post-Darwinian economics” (see Edgell, 2001, p.68). As he remarks:

“The characteristic feature by which post-Darwinian science is contrasted with what went before is a new distribution of emphasis, whereby the process of causation, the interval of instability and transition between initial cause and definitive effect, has come to take the first place in the inquiry; instead of that consummation in which causal effect was one presumed to come to rest” (Veblen, 1961 [1909a], p.37).

In other words it could be argued that in Veblenian thought pre-Darwinian science is characterized by the process of description of effects while post-Darwinian science by the process of causation of effects. In these terms the role of economics changes, from the analysis of economic behaviours and their effects within a natural order of natural law to an analysis of causation and continuous changes – “self propagating and self continuing” changes (Veblen, 1964 [1919b], pp.36-37) – of social habitat and their impact on individual economic behaviours (see Edgell, 2001, p.68)⁵. On this point Hodgson (1998, p.419) remarks that Veblen rejects neoclassical economics since it does not “contain an evolutionary explanation of the origin of the assumed behavioural characteristics”; for example - Hodgson (1998, p.419) adds – in the neoclassical theory of consumption the explanation “on the origin and initial acquisition of [...] preferences” is completely absent [and] the assumption that individuals are selfish requires an explanation of the evolution of selfishness” (Hodgson, 1998, p.419; see

⁵ On Veblenian Darwinism see also Harris (1934), Hofstadter (1945), Murphree (1959), Dewey (1967), Sowell (1967), Russett (1976), Mayhew (1987), Edgell and Tilman (1991), Hodgson (1994).

also Tilman, 1999). Edgell (2001) tries to identify the conditions for which Veblen is certainly identifiable as a post-Darwinian. As he argues - Veblen's economic theory incorporates some "key Darwinian elements [that is to say:] variability, *struggle for existence* and *natural selection*" (Edgell, 2001, p.69; italics added). More specifically, as remarked by Edgell and Tilman (1989), there are three key principles of Darwinian theory that affect Veblen's theory: a) "species vary enormously", b) "species tend to reproduce on a scale that precludes the survival of all but the *fittest*", and c) "in the ensuing struggle for existence, *the variations that are best adapted will survive*" (Edgell and Tilman, 1989, p.1005; italics added). Such inspiring principles allow Veblen – as Tilman (2003, p.xviii) remarks – to build an economic theory as the "science of collective welfare" in other words as "a [science] of advancing the instrumental adaptive powers of the entire community to ceaseless change". In addition Dugger (1979, p.426) remarks that the idea of "post-Darwinian economics" in Veblen's thought can be seen as a Darwinian combination of the main schools of evolutive processes: a) "progressionism" and b) "uniformitarianism". Let us look more closely at this point: as Eiseley (1958, p.353) argues, by progressionism "life has risen from simple to more complex forms throughout the successive eras of the geological past [while uniformitarianism states] that geological phenomena were the product of natural forces operating over enormous periods of time and with considerable [...] uniformity". Following these concepts, Dugger (1979, p.426) remarks that just as Darwin supplied progressionism with the principle of natural selection – demanded by uniformitarianism – so Veblen supplies social progressionism with the principle of institutional change via social uniformitarianism. In fact inspired by Darwinian principles, Veblen would build his theory of institutional change (see ch. 3) in terms of cause and effect of the succession of great cultural eras substituting – as remarked by Edgell and Tilman (1989, p.1005) – "the concept institution for Darwin's reference to species". In this sense Anderson writes: "the several [social eras described by Veblen] are admitted *to be not sharply separated*; they are supposed to be marked off only roughly according to *certain characteristic features*" (Anderson 1933, p.605; italics added).

b) *The indefinable causation approach*. His studies of the origin of economic phenomena are based on a strong interdependence between micro and macro matters. With particular reference to his studies on human nature and behaviour Veblen writes:

“The individual is a creature of *heredity* and *circumstances*” (1922 [1914], p.139; italics added). In these terms Veblen sees human beings and their current behaviour as the outcome of traits and behaviours inherited from the past and of traits and current behaviours. Consequently current micro traits and behaviours are outcomes of current and past social traits and behaviours, just as current social traits and behaviours are outcomes of the past and current micro ones. As Hodgson (1998, p. 419) remarks, at the same time Veblen rejects “the proposition that the individual is *exclusively* a social [outcome]” or that s/he is completely exempt from social influences. So in Veblen a static and ‘natural’ vision on human nature does not exist and – it could be added – *it is not necessary for it to exist* insofar as economic behaviour is an institutional product, no ‘natural’ law being admitted. As Hodgson adds: “there is both upward and downward causation; individuals create and change institutions, just as institutions mould and constrain individuals” (in Davis *et al.*, 2004, p.87)⁶. In opposition to Hodgson’s interpretation others point to the holistic nature of Veblen’s methodology as his distinctive trait as regards the methodological individualism of neoclassic economics. Bush (1999, p.134) maintains that Veblen’s methodology can be regarded as holistic, where holism is defined in the following terms: “A holistic methodology [...] rests upon the view that [...] facts can be derived from an analysis of socially prescribed patterns of correlated behaviour (i.e. institutions), which are both the determinants and consequences of individual behaviour in a complex, evolving relationship”⁷. Coats (1954, p.532) also looks at Veblen’s methodology in holistic terms since “Veblen’s [society] is a type of [society] in which the forces of heredity and environment are given primacy over human rationality”.

b) The critique of neoclassical hedonism. It is well known that neoclassical economics structures its theory assuming that after having collected information and elaborated it, all individuals rationally structure their own actions so as to have maximum pleasure (gains) or minimum pain (costs) – the ‘*hedonistic*’ aim – in a given

⁶ Veblenian human nature is in fact a mix of social and individualistic aspects where the predominance of one aspect rather than another one can be ‘obscure’ in its origin but not in its effects. For example – as will be shown more clearly below – while the origin of an instinctual is not particularly clear in Veblen, its effect instead is clear and significant, in particular on topics like institutional changes, economic growth and income distribution.

⁷ On the other hand, the same author describes methodological individualism in the following terms: “Methodological individualism prescribes an atomistic view of society based on the premise that any meaningful proposition about social phenomena must be reducible to the logic of individual choice-making” (Bush, 1999, p.133).

context which it is not necessary to investigate⁸. Contrary to such a vision, Veblen identifies two particular problems of sustainability of neoclassical ‘hedonism’: *a)* the oversimplification of the causes of action, *b)* the oversimplification of the environmental context. In fact Veblen is not mainly interested to making a critique of hedonism itself. Hedonism conceals an element on which he is in agreement since he too views human action in terms of action *with a design*. The matter on which Veblen focuses critically is the construction of human conduct by which human beings reach their aim. In other words the critical point of differentiation between the neoclassical school of that period and Veblen concerns the sense of intelligent conduct, in other words the sense and meaning of rationality. For neoclassical economics an intelligent choice coincides with a rational action. In particular a rational action must lead the individual to reach her/his ‘hedonistic’ aim by an objective, deliberate and exhaustive procedure which – starting from a perfect knowledge of the *cause* of an action, that is to say the sensations of pleasure and pain – involves an optimum certain or foreseeable *effect*. His studies on human behaviour instead raise two main questions: one connected to the cause of an action and the other to its effects. In other words the sensation of pleasure and pain can be a cause of action but it is not the only one. Often instinctual behaviours find their foundations in causes that are different from pleasure or pain. Obviously if the cause is not simply identifiable as pleasure and pain then the effect of action cannot be simply the reduction of pain or the increase of pleasure. On the other hand the matter of environmental influence is expressly investigated by Veblen (1961 [1909a], pp.234-236). As Hobson (1937, p.140) remarks: “To present economic man as a rational being, calculating and regulating all his activities in terms of conscious costs and satisfactions, falsifies the actual situation, for it requires the suppression of facts and activities which intimately interfere with the hedonist calculus”. Tilman (2003, p.xiv) has recently argued that: “Veblen criticized the hedonistic [...] theory for portraying humans as passive agents reacting to external forces only when impinged upon”. So he is in agreement with the interpretation of Anderson (1933, p.601; see also Hobson, 1937, p.141) who identifies the neoclassical agent in Veblen as “a passive creature who reacts only to external stimuli in a mechanical sort of way”. Actually Veblen sees such an individual not as an agent. He

⁸ As known, Bentham (1969 [1780], p.86) identifies hedonism as “that property in any object, whereby it tends to produce benefit, advantage, pleasure, good, happiness”. For a reconstruction of the literature on rationality in economics see amongst others Sacco and Zamagni (2002) and Davis, *et al.* (2004).

often calls her/him “absorbent” or “defective subject” (Veblen, 1898a, p.189). The idea of the neoclassical agent as a passive agent requires an explanation of the significance of external conditions for such an approach and a comparison with Veblen’s vision. In a hedonistic logic the external context is not an integral part of life for each individual and therefore of her/his choices. In other words, the external context is just a constraining context against which the individual *reacts*. It is not like the context in which the individual moves and *acts* for Veblen; in other words while hedonism is based on a logic of ‘*reaction to*’, where incentives/disincentives (in terms of the opportunity-cost of the action) are the sole forces which prompt reactions, Veblen stresses that economic behaviour rests on the ‘*active propensities*’, i.e. actions not (necessarily) driven by external stimulus. Moreover Veblen shows his own sense of rationality in a different manner. As Bush (1999, p.138) writes: “human beings are rational [for Veblen] in the degree to which they can evaluate their behaviour according to whether it enhances the life process taken impersonally”. In other words Veblen sees rationality in terms of critical evaluation of current institutions. Obviously such a sense of rationality is completely different from the neoclassical meaning and it is instrumental to institutional change (see ch.3). So according to Bush (1999, p.139) the Veblenian concept of rationality is prevalently dynamic, not static. In other words it evolves with the changing of the “specific content of the [...] concept of what enhances the [human life]” whose changing is a matter of “changes in the environment, [...] growth of knowledge, [...] technological innovations, and [...] contact with other cultures”. Bush (1999, p.138) also adds that the Veblenian rationality is not the “precondition for the exercise of [self-interest] in the fulfilment of one’s desires but for its “self-restraint”. Two points Bush raises are: *a*) the individual prevalently acts on the basis of experience since “self-restraint” is objectively possible if the individual has “learned [her/his] behaviour” (Bush, 1999, p.139), *b*) rationality has a cultural dimension (see also Waller, 1988, p.118; Hodgson, 1998, p. 419)⁹. Looking more

⁹ The modern institutional literature emphasises the realism of hypotheses rather than their axiomization (see Vanberg, 1993). So as Forges Davanzati remarks (2006a, p.81) the neoclassical model of rationality should be revised on the bases of the following main variables that affect the decision-making process, namely: culture, experience and uncertainty. However apart from the range of social and psychological variables that could be taken into consideration, the main point on which institutionalists agree is that – as Forges Davanzati (2006, p.83) writes – “no unique motivation of human behaviour is assumed” and “the economic problem is not [necessarily] a problem of allocation of scarce resources among different exogenous uses” and external contexts are not simple constraints since they represent “relevant or irrelevant situations” (Forges Davanzati, 2006, p.84). It is important to notice that unlike the neoclassical model, institutionalism is still lacking in the definition of an organic

closely, Veblen defines culture thus: “[culture] is a complex of habits of life and thought prevalent among the members of the community (Veblen, 1961 [1908c], p.39)¹⁰. As Bush (1999, p.139) writes: “All cultures begin inculcating their young at the earliest possible age with a sense of the individual’s obligation to the well-being of the group. It is through this learning process [...] that such rationality becomes habitual”. The main matter connected to the cultural dimension of rationality is the quantity and quality of information that each individual needs for structuring her/his decision-making process. In fact the question of the cultural dimension of rationality is a matter of knowledge. More specifically, Veblen assumes that “human logic” (Veblen, 1964 [1919a], p.7) and the conduct of individuals is structured on the basis of knowledge and belief. Knowledge and belief are institutional matters since they include “convention[s], inference[s] and authentic opinion[s]” (Veblen, 1922 [1914], p.39) which represent those circumstances in which culture is formulated (see Coats, 1954, p. 534). Knowledge is the complex “of principles governing what is fact” while belief is the complex “[of principles governing] what is credible” (Veblen, 1964 [1919a], p.6). Knowledge and belief necessarily affect behaviours since these principles supply suggestions about “what is to be done” and “how it is to be done”. So knowledge and belief become matters of experience and theory. Moreover no human action is completely based only on knowledge or belief. In fact action is often a mixture between the two components but the prevalence of one component over the other is instinctual and a matter of habits (cf. Weed 1972). Moreover if the cultural dimension affects rationality then rationality changes over time. Let us explain why: Knowledge and belief are social outcomes¹¹; they are outcomes of institutions and consequently they are institutions themselves and like other institutions, knowledge and belief are subject to “revision and correction by experience” when conditions of

and coherent alternative model of behaviour (see Costabile, 1998 for a general picture on contemporary institutional theories). Many authors in fact limit their analysis to the demonstration of the critical points of the neoclassical model often by empirical or psychological simulations (see for example Marglin, 1974; Kahneman and Tversky, 1979; Camerer, 1997; Van Staveren, 2001; Reisman, 2002; Schmid, 2004).

¹⁰ Unlike Mitchell (1973 [1929], p.610) who remarks that culture is in fact the consequence of the modality of consumption of time. Investigating the habits of thought – and therefore culture – is equal to investigating the modality in which individuals spend their time.

¹¹ In fact when Veblen writes that “blind persons do not build colour schemes” he wants to point out that they cannot have knowledge or belief about colour schemes precisely because colour schemes are outcomes of a social convention to which these persons unfortunately cannot conform. In the same way he adds “nor will a man without an ear for music become a master of music composition (Veblen, 1964 [1919a], p.6). Music is conventionally accepted as being catchy and only a musician who is able to conform to such a convention becomes a master.

life change (Veblen, 1964 [1919a], p.7) and consequently also rationality changes. Ries (1964) instead sees Veblen's meaning of rationality in a more pragmatic sense. As he writes "rationality for Veblen meant the adaptation of technical means for the most efficient achievement of the ends of production"¹².

¹² In the above sections the Veblenian idea of economics and its differentiation from neoclassic economics has been described. However it is important to notice that when he makes critiques of *current* economics (first of all as regards John Bates Clark) he looks at both classical and neoclassical economics without a precise differentiation between the two schools. It is interesting to understand in what terms Veblen refers to the classical and the neoclassical approach. On this topic Aspromourgos (1986) and Fayazmanesh (1998) agree that concepts of classical and neoclassical economics are not very clear in Veblen. They also agree that Veblen uses hedonism as a merging criterion between the two approaches. What they disagree on is the sense and correctness of the term 'neoclassical' in Veblen. In particular Aspromourgos argues that – by the term neoclassical economics – Veblen's intent was to attribute a theoretical continuity between classical economists and marginalists, who may differ on the methodological plane but not in the underlying principles. Aspromourgos therefore takes up the case put forward by Anderson (1933, p.600) who writes: "According to Veblen's analysis of the development of economic thought, the theory of today is substantially an elaboration of the English classical doctrine. [...]". So neoclassical economics becomes the natural and cumulative development of classical economics. However, Fayazmanesh stresses that even if Veblen's intent is to convey a continuity between classical economists and marginalists with the term 'neoclassical economics' he in fact fails to do so; Fayazmanesh argues that Veblen in fact confines himself to showing a certain similarity rather than a continuity between the two approaches. The consequence is that – he writes (1998, p.75) – "this makes the term neo-classic [in fact] unnecessary and as result Veblen himself abandons the use of the term" substituting the term neoclassical with the term "post-Bentham economics" (see Veblen 1961 [1899d], p.132). Fayazmanesh (1998, p.75 and ff.) then adds that the aim of common identification of the two approaches is built by Veblen on the wrong premises since: *a*) he interprets classical and marginalist thought in a superficial manner, *b*) in fact he coins a term (neoclassical) with the purpose of clarifying the description of the evolution of economic thought but concretely just produces confusion originating from the aim of classifying classical and marginalist theories merely by the hedonistic criterion (see also Cornehl, 1969) which, in addition, was not clearly identified by the same author. Veblen - Fayazmanesh (1998, p.79) argues – limits himself to adapting the hedonistic criterion to each author rather than verifying the objective congruity of each theory to his criterion. For example with reference to Adam Smith, Fayazmanesh (1998, p.75) argues that Veblen makes reference to the sense of Smithian utility or "value in use" in terms of usefulness and therefore in terms of "serviceability". Bush (1996, p.3, in Fayazmanesh, 1998, p.80) tries to explain why Veblen considers Smithian serviceability in hedonist terms, supplying the following answer: since Smithian serviceability can be seen both in an objective and subjective way, then it is perfectly within the hedonistic logic. In contrast, Fayazmanesh (1998, pp.80-85) gives a different answer: Veblen does not principally look at the nature of utility in Smith but mainly at his theory on the goals of human action. So the Smithian logic of self-interest is the criterion by which Veblen assigns Smith the label of 'hedonistic economist', actually confusing self-interest and hedonism. In fact on this point Veblen writes: "In hedonistic theory the substantial end of economic life is individual gain" (Veblen 1961 [1899d], p.139). At the same times Veblen tries to adapt hedonism to other classical authors such as Marx, assuming that the author looks at the nature of class struggle in terms of self-interest (see Fayazmanesh, 1998, pp.85-88) and in Ricardo for his "uncritical[...] acceptance of the metaphysics comprised in the common sense of his time" (Veblen, 1961 [1899d], p.131 footnote 23).

1.2 The theory of instincts and institutions

1.2.1 *Instincts*

According to Veblen, all individuals are affected by two kinds of aptitudes: *a)* the “instinctive proclivities” – *instincts*, *b)* the “tropismatic aptitudes” – *institutions* (Veblen, 1922 [1914], p.1)¹³. The difference between these two aptitudes can be interpreted in the following terms: *a)* instincts are *directional aptitudes*, that is to say aptitudes towards the definition of contexts while *b)* institutions are *response aptitudes*, that it to say aptitudes towards re-actions, in other words they are aptitudes of response to contexts. So while instinct becomes a directional aptitude from the individual towards a context, the institution becomes a directional aptitude from a context towards the individual. The predominance of a particular institution is the effect of the prevalence of a particular instinct. On this point Veblen writes:

“A genetic inquiry into institutions will address itself to the growth of habits and conventions, as conditioned [...] by the innate and persistent propensities of human nature; and for these propensities [...] no better designation than the time-worn “instinct” is available” (Veblen, 1914, pp.2-3).

Even if all individuals structure their conduct on the basis of instincts and institutions this does not mean that instinct and institutions are simply individualistic matters. These variables of conduct can be also variables of social conduct and in particular variables of conduct of particular social classes in which the individual is allocated. In Veblen’s vision different social classes are formed by individuals with the same instincts and institutions, and the peculiarity of such instincts and institutions structures the features and behaviour of the social class itself. In view of this it could be argued that individuals – on the whole – are involved with different instincts for three main reasons: *a)* each instinct manifests itself with distinctive aims to be attained and considered as “the ends of life” (Veblen, 1922 [1914], p.5), *b)* different individuals are involved with a shared instinct, finally *c)* each individual is involved with different instincts. Given the above premises let us see two particular aspects of Veblenian instincts:

¹³ It is important to notice that unlike the common vision Veblen speaks about institution in terms of habits of thought and not directly in terms of rules, organizations and customs. In the present work the term institution and habit of thought will be used as synonymous, in line with Veblen’s original definition.

a) The origin of instincts. A problem not explained by Veblen is the origin and predominance of a given instinct. Two possibilities can be taken into account: *a)* instinct has a biological origin, *b)* instinct has an institutional origin itself. Veblen defines instincts as *teleological native proclivities* that is to say “native proclivities [or stimulus which] set up a characteristic purpose, aim or object to be attained” (Veblen, 1922 [1914], p.3; see also Veblen, 1961 [1898c], p.75). The ‘teleological’ character of instinct allows Veblen to view the same instinct as a conscious and adaptive propensity – “activity” – towards “an end aimed at”. One could argue that Veblen rejects the idea that instinct *always* expresses itself in mechanical and biological terms as “movements of orientations” (Veblen, 1922 [1914], p.4) since the instinctual activity is not independent of will, reasoning and emotion. However Edgell (2001, p.79) maintains that the individual will, reasoning and emotion is not incompatible with the biological nature of instinct. As Edgell (2001, p.79) writes “instincts for Veblen [are] biological” and differ from animal instincts for the high degree of intelligence with which the human species manage and control them. On the other hand O’Hara (1999, p.162) states that “instincts, for Veblen, are not purely physiological, biological, and psychological, but are heavily conditioned by institutions”. In the same way Asso and Fiorito (2003, 2004, p.448) remark that “[...]instincts [were seen as] propensities *inborn* in the human agent and transmitted as hereditary traits”, but that the sense of the “hereditary trait” is not biological. Interpreting Veblen the authors adds that instincts were not actually seen as direct and simple reactions to impulses but mainly as “intelligent adaptations towards selected ends”. Hence instincts required natural and spontaneous observation, analysis, calculus and decision about the goal to be reached. According to O’Hara the interpretation on the biological nature of instincts can be interpreted correctly if Veblen’s theory of instincts is combined with his theory of institutions. In other words the origin of instinct must necessarily be biological but – in an evolutive process – it necessarily combines with the pressure of institutions; as a result, habits of life – affecting habits of thought – also affect human intelligence which then affects the instinctual traits of the human species. In these terms Veblen in fact considers institutions as outcomes of instincts, probably at the outset of the evolutionary process, but then the causal relationship changes from instincts-institutions to institutions-instincts.

The interpretation presented by O'Hara allows us to understand better the interpretative mistakes of Frank Knight who made a critique of theory of instincts in the 1920s. As remarked by Asso and Fiorito (2003, 2004) Knight argued that the theory of instinct would be useful for economics if instincts as a whole were enumerable and describable. It is important to notice that Knight interpreted the origin of instincts only in biological terms so his critique seems to be affected by a misunderstanding of the Veblenian theory of instincts. In fact he stressed that since instinct has a biological nature and is in constant evolution nobody is capable of defining a closed set of instincts which in turns appears to be a necessary condition for describing the logic of a behaviour in the sense that a closed set of instincts can correctly represent a set of hypotheses from which economists can elaborate a universal law about behaviour (see Knight, 1922, p. 467). In addition to this methodological criticism of the instinct theory, Knight adds that economic behaviours are not biological since they are often led by mystical expectations and by "cultural canons". On this point Knight writes: "Wants are culture products, to be judged by culture canons and understood and controlled through culture categories. Even our food and clothing, in all their concrete content, and by far the larger part of their money cost, represent social and aesthetic and not biological value" (Knight, 1935, p. 95; italics added; see also Knight 1924, 1935, 1956 [1951], 1960). The above quotation seems to have more elements in common with Veblen than elements of opposition. In fact if instincts are seen as the outcome of institutions then the Knightian idea of behaviours as outcomes of culture is perfectly consistent with the Veblenian idea of behaviours as the outcome of habits of thought.

On the interpretation of the origin of instinct Rutherford (1984, p.332) remarks "it must be understood that in Veblen's system the instincts, except in the earliest phases of cultural evolution, do *not* have a major role in determining or shaping the institutional structure. For him, human behaviour is [...] a matter of institutions [...] which are not the direct [...] products of the innate propensities of human nature". So Rutherford does not see the origin of institution in terms of instincts. Referring to *The Instinct of Workmanship* (1898) and *The Engineers and the Price System* (1921) Rutherford stresses that institutions originate in the "methods of livelihood that prevail[...] at [a given] time" (Rutherford, 1984, p.333) rather than in instincts. In other words, following Rutherford (1984) it is possible to say that in the Veblenian view an

institutional system is the outcome of a material system, that is to say it is a system of habits of action and thought that develop within a system formed by “material, technological and economic means” (Rutherford, 1984, p.333). One could argue that such an observation does not concretely explain the origin of institutions since the material system in Veblen’s vision is a human outcome not a natural one; in other words the material system is an instinctual and institutional outcome itself. Dugger (1979, p.430; italics added) for example writes that in Veblen’s thought “people, *not divine forces*, shaped institutions but institutions also shaped people”. In conclusion, in view of the above it can be said that a clear explanation of the origin of instincts and consequently also of institutions is not clear in Veblen and different interpretations have been presented by the literature without completely clarifying the question.

b) *The rationality of instincts*. Though, as has been said above, instinct is therefore a conscious propensity. Instinct is a conscious propensity because individuals know their own traits and act within them. In other words instinct is a complex proclivity and the impulsivity of action is not its main feature. On the contrary Veblen attributes the feature of activity to instinct and an activity cannot be impulsive since it calls for reasoning, thought and feelings. As Veblen writes:

“[Man] acts, so he [always] thinks and feels. This is necessarily so, since it is the agent man that does the thinking and feeling” (Veblen, 1898a, pp.192-193).

The above consideration appears clearer in the following passage:

“The agent moved by its impulse not only runs through a sequence of actions suitable to the instinctive end, but he is also given to dwelling, more or less sentimentally, on the objects and activities about which his attention is engaged by the promptings of this instinctive propensity” (Veblen, 1922 [1914], p.53).

It is interesting to notice that Veblen builds his theory of instincts in line with the state of the cognitive sciences at his time. As Cordes (2005, p.7) writes: “In contrast to the modern ethological understanding of ‘instincts’, Veblen’s notion of them does not involve more or less fixed behaviours but a bundle of flexible dispositions or propensities that can be suppressed or diverted” (see also Wolozin, 2005).

So according to Veblen, instinct is 'rational' since it is conscious and has a design but its goal is different from the neoclassical goal. In fact the neoclassical goal is simply represented by the 'hedonistic' aim. In the first case the aim of actions is freely determined *a priori* by the agent while in the second case instinct shows itself as a stimulus determined *a priori* by itself. So the 'rationality' of instinct is principally a matter of intelligent management of the same in a non-impulsive way. In fact while "the purposes to be achieved are assigned by man's instinctive proclivities [...] "the ways and means of accomplishing those things [...] are a] matter of intelligence" (Veblen, 1922 [1914], pp.5-6) where intelligence is not a biological matter but an institutional one. As Veblen remarks:

"In an eminent sense [the individual] is an intelligent agent [in other words] man is an agent, not an absorbent; he is an agent seeking in every act the accomplishment of some concrete, objective, impersonal end" (Veblen, 1898a, p.188-189).

In particular Veblen defines the agent in the following terms: "[s/he] is a coherent structure of propensities and habits which seeks realisation and expression in an unfolding activity" (1961 [1898c], p.74). The ends of life – to which instincts direct actions - are different for a given group of individuals. Even if the ends of life depend on instincts their actual achievement realistically depends on external conditions. External conditions in fact represent a kind of constraint on the free manifestation of the instincts themselves and therefore on the full realization of the end of life. The external conditions to which Veblen makes reference are prevalently social constraints; in other words, external conditions are imposed by the presence of other social groups, so they are imposed by the *incompatible* presence of each instinct with others, as well as of each institution with others.

As Veblen remarks, individuals live in an unfriendly *habitat* mainly due to the presence of limited resources¹⁴. Living in an unfriendly habitat requires intelligent actions, in other words "intelligent" uses of instincts (Veblen, 1898a, p.188). The

¹⁴ Veblen does not make reference to the scarcity of resources in natural terms. In his idea resources are kept scarce. The behaviour of undertakers on the under utilization of capital (see below) is a clear example. However the idea of natural scarcity of resources is not completely excluded by the author. When he tries to explain the evolution of instincts and institutions (see below and ch.3) in fact he seems to make reference to the natural scarcity of resources. In particular the instinct for efficiency – workmanship (see below) – is explained by Veblen as the first instinct of the human species since it was the "intelligent" answer to the adversities of the natural environment surrounding the individual.

individual is an intelligent agent if s/he gives concrete form to the instinctual action by a “concrete, objective [and] impersonal” tool: the institution. The intelligent use of instinct – therefore the adaptation to the corresponding institution – is therefore able to bring the outcomes which are recognized as ends of life: survival, excellence, and creation.

1.2.2 *The institutional dimension of individual action*

Mayberry (1969, p.316) stresses that Veblen identifies institutions from two points of view: *a)* “from a psychological perspective they are habits of thought and life”; *b)* “from a social point they are [habitual processes of management of social life]”. In fact the two points are interdependent in Veblenian thought and as for each other aspect of his theory it is not clear which aspect prevails over the other. With reference to the previous section, a fundamental consideration must be made: while the ends of life are imposed by the social evolution of classes – constituting an instinctual matter – “the logic of ways and means” for replying to the stimulus is an institutional matter (see Veblen, 1922 [1914], p.6). The intelligent use of instincts in fact depends on “the available body of knowledge”; since knowledge is a matter of thinking and experience, then intelligence is “a matter [...] of *habits of thought* accumulated through the *experience*” (Veblen, 1922 [1914], pp.6-7; italics added). Consequently, institutions at the same time furnish: *a)* information and *b)* a mental methodology of choice based on the use of common attitudes and on ‘natural’ predispositions in acting and thinking in a well-defined and regular way. An attitude of thought and action becomes an institution when an individual as well as a group gives the role of *spiritual* or *practical guide* to it by a process of use, repetition and/or imitation – *normalization* - and this happens when individuals attribute an authoritative character to it – Veblen’s *legitimation* (see Veblen, 1975 [1899a], p.212).

It is possible to look at institutions in terms of *normalized* and *legitimated* habits of thought (Veblen, 1975 [1899a], p.190) and habits of life (see Veblen, 1967 [1923], p.101); in other words they are *styles* of behaviour and reasoning. It is important to point out that Veblen sometimes sees habits of thought and habits of life in a parallel sense, sometimes in an interdependent sense and sometimes in a

dependent sense. In fact in the *Theory of the leisure class* Veblen defines institutions precisely in terms of habits of thought. As he writes:

“The institutions are [...] prevalent habits of thought with respect to particular relations and particular functions of the individual and the community” (Veblen, 1975 [1899a], p.190).

He also sees institutions alternatively as habits of thought produced by habits of life and *vice versa*. However, Veblen often considers institutions only as outcomes of routine habits of life and sometimes as outcomes of routine habits of thought. He writes:

“An institution is of the nature of a usage which has become axiomatic and indispensable by habituation and general acceptance” (Veblen, 1967 [1923] p.101, footnote 1).

But he also remarks:

“The habits of thought which are [...] formed under the guidance of teachers and scholastic traditions have an economic value – a value as affecting the serviceability of the individual – no less real than the similar economic value of the habits of thought formed without such guidance under the discipline of everyday life” (Veblen, 1975 [1899a], p.363).

However it is important to notice that habits of thought and habits of life do not automatically constitute an institution. As Edgell (1975, p.272) comments, only “when habitual thoughts and actions become established and patterned over time” do they become institutions. As a result, it is not sufficient to have a habit to have an institution; it is also necessary for it to be normalized and legitimated. By what mechanism does a habit become normalized? According to Veblen normalization of conduct and thought can be considered an instinctual and/or educative and/or coercive process (see Veblen, 1975 [1899a], p.212). Moreover, the normalized habit needs legitimation. Interpreting Veblen one could argue that in fact the mere use of an institution is the cause-effect of its legitimation. Using an institution means conferring legitimation upon it but an institution is used because it has been legitimated. So an institution can exist only if it is used and the use of an institution automatically credits it as a right and good norm. The legitimation of an institution is not necessarily natural since it may be imposed; it might therefore suffer from elements of immorality but the

continuous utilization of the same institution in fact eliminates such elements, conferring complete morality upon it. In addition, Veblen comments:

“What men can do easily is what they do habitually, and this decides what they can think and know easily” (Veblen, 1898a, p.195).

It could be argued that Veblenian institutions have the nature of particular methods of simplification of cognitive/decisional processes. In fact institutions simplify this process in a double and interdependent way: *a)* predisposing individual decisions and *b)* predisposing individual actions. The predisposition of a cognitive/decisional process is simply a matter of use of the institution. Such a process is not necessarily based on a methodology of reasoning and calculus. In particular Veblen points out that reasoning and individual calculus count for little as regards the weight of habits. It could be argued that this relative weight is also due to the fact that reasoning and individual calculus is in fact an institutional outcome. However it could be added that institutions play the part of a *mental trainer* in the sense that they *lighten* the mental effort – needed for taking a decision and then acting – training human cognition towards the regular use of thoughts and actions. Allowing a saving in mental effort allows the individual to save effort in collecting information, assessing it and elaborating it since “[men] feel at home in the range of ideas which is familiar through their everyday line of action” (Veblen, 1898a, p.195).

Scholars have been particularly interested in investigating the dynamic or static trait of Veblenian theory of institutions. On this topic, two contrasting interpretations can be traced: the *evolutionist* interpretation and the *social order stability view*. This distinction pertains to those who prevalently sustain the Veblenian theory of institutional change – focusing on the dynamic aspect of social order – and those who oppose it, supporting the Veblenian theory of social inertia, and therefore mainly focusing on the static analysis of social order.

A curiosity concerning the original title of his main work seems to show a ‘strange change’ in Veblen, who seems to move from one direction towards another, even though this oddity has not been clearly explained by the literature. As Edgell (2001, p.77) – referring to Dorfman (1934, p.232) – remarks – *The theory of the leisure class: An Economic Study of Institutions* (1899) – was originally subtitled *An Economic Study of the Evolution of Institutions* and the subtitle was changed only in

1912. Why this happened is not clear. It may simply have been a stylistic change but the elimination of the term 'evolution' may conceal Veblen's explicit intent to formulate a static theory of institutions. On this point Edgell - referring to Dorfman - simply argues that the subtitle changed "on the occasion of the [new] publication" (Edgell, 2001, p.77) which was "a special cheaper edition" (Dorfman, 1934, p.323). In the absence of adequate sources no particular or original interpretations can be put forward.

As remarked by Rutherford (1984, p.331): "a number of commentators on Veblen's work on the processes of institutional change have concurred that for Veblen institutions are static, backward looking, and resistant to change, alterations in the institutional structure occurring only under pressure from the dynamic of technological process" (see for example Teggart, 1932; Riesman, 1960; Hamilton, 1970; Walker, 1977; Viano, 2003). At the same time Rutherford (1984, p.334; italics added) himself sustains the evolutionary aspects of Veblenian theory stressing that: "Veblen, [...] did not present his evolutionary schema in a general or abstract fashion, but the same sequence of processes is repeated throughout his treatment of *institutional history*". In this second case, a rationale for the possible institutional stability is needed. Eby (1998, p.691), interpreting Veblen, tries to reply in the following terms: each institution always enjoys a "relative stability" in the sense that "institutions cause established behaviours and social structures to seem natural and therefore correct". In other words "the relative stability" manifests itself first in an *self-sustaining* sense; in Veblen's thought in fact institutional change cannot be immediate since it is an outcome of habits and as we have said a habit becomes an institution when it is *normalized*; normalization in turn requires time because the same action and thought must be continually repeated and when it is normalized it becomes "natural" and "correct". Next, this self-sustaining process Eby (1998, p.691) also adds an external factor which she describes thus: "institutions also confer power on groups of people whom Veblen refers to as 'vested interests', allowing them to exploit the generic public or 'common man'". As Forges Davanzati (2006a, p.54) points out, "inertia is seen [by Veblen] both as psychological - as "instinctive resistance" (Veblen, 1975 [1899a], p.203) and as a social phenomenon". With reference to the psychological aspect of inertia, Veblen writes: "The aversion to change is in large part an aversion to the *bother* of making the readjustment which any given change will necessitate"

(Veblen, 1975 [1899a], p.203; italics added). On the other hand, on the social plane inertia has an economic foundation: the distribution of income in favour of the leisure class.

It is interesting to notice that the static analysis of institutions is particularly evident in those points in which Veblen describes the current situation, that is to say the nature and effects of pecuniary culture. Inertia therefore becomes instrumental to his critique of the current state of things. Thus Veblen uses the concept of social inertia as an expression of his pragmatic attitude to the critical description of his current situation. As Mayberry (1969, p.316) remarks – on institutional inertia – that “habits of thought would persist indefinitely if circumstances did not force a reappraisal of the facts”. The *current* facts described by Veblen show such a situation. For this reason as Eby (1998, p.689) points out, inertia is a Veblenian form of speculation on “the causes of social stagnation”. In brief in Veblen’s thought, institutional development is the rule and it could be argued that social inertia represents the exception to the rule: “the question [Veblen writes] is not how things stabilize themselves in a static state, but how they endlessly grow and change” (Veblen, 1925, p.51).

1.3 The social order

Veblen’s picture of the macroeconomic process as well as of class distinctions and the relative function is to be mainly traced in *The theory of the leisure class*. Two peculiar features characterize the Veblenian macroeconomic system: *a*) it is a credit economy (see § 2.1), and *b*) it is a conflictual economy (see § 1.4). Moreover Veblen structures an economy in which different social classes (or groups) are involved: *a*) the leisure class, *b*) the undertakers, *c*) the technicians, and *d*) workers. These classes work within a system ruled by a State – “that is to say the government” (Veblen, 1904, p.284) – which is identified by Veblen as an institution representative of the prevalent habits of thought in the society. More specifically analysing the *current* traits of the State Veblen remarks as:

“The ring of *business interests* which secures the broadest approval from popular sentiment is, under constitutional methods, put in charge of the government establishment [...]. But the only secure basis

of an enduring party tenure of the government machinery is a *business policy* which falls in with the interests [...] of the effective majority” (Veblen, 1904, p.294; italics added).

Veblen studies the traits of the State in the specific form of “constitutional government and parliamentary representation” (Veblen, 1904, p.284). Since the State has the form of a representative Parliament, different social classes can manage it, but the logic of its management is always the same: “the business policy” to sustain the social class that is mainly represented. More specifically the social class mainly represented in the *current* organization of the State, according to Veblen is that of business men, therefore both the members of the leisure class and undertakers (see below). As he writes:

“Representative government means, chiefly, *representation of business interests*. The government commonly works in the interest of the business men [...]. Government has, in the main, become a *department of the business organization* and is guided by the advice of the business men” (Veblen, 1904, pp.286-287; italics added).

It will be argued in section 3.3c that the State plays an important role in whether or not the existing social order is maintained. On the role of the State in Veblen’s thought see Mouhammed (2003) who emphasises that the State is involving in preserving the interests of the kept classes. Moreover O’Hara (2004, p.979) has recently argued that “Veblen recognized that politics and economics were two aspects of a unified social whole to be understood together. The State is the guarantor of the existing social order and protects existing property rights and the interest of the leisure class [...] Veblen made it very clear that the interests of the capitalist absentee owners are the primary concern of the government”. In the prosecution of the discussion about social order the analysis of the State will not be taken into consideration since in fact Veblen does not see the State as a different organization independent from the existing social classes but as the “department” of some class. So it is sufficient to investigate the traits of the social classes to also automatically have the traits of the State, since it is representative of the interests of the main representative class.

The originality of Veblen’s social order is not the description of features and functions of social classes but mainly his attempt to attribute instincts to them rather than to single individuals. In his writings Veblen identifies the following main groups of instincts: *a)* the predatory instinct, the salesmanship and the pugnacity that present

similar features and are attributed both to the leisure class and undertakers, *b*) the instinct of workmanship and idle curiosity that are attributed to technicians, *c*) the instinct of survival of the lower classes and finally *d*) the parental bent and the instinct of solidarity and sympathy which are attributed to all classes. It is possible then to add that the ends of life of the social classes are: *a*) survival for low classes, *b*) creation for technicians, finally *c*) excellence for kept classes: the leisure class and undertakers (Veblen, 1964 [1919a], p.162; see also Veblen, 1975 [1899a], p.229). Commentators have tried to identify some of the criteria followed by Veblen in cataloguing instincts. Edgell (2001, p.82) for example uses the parameter of *benefit* as a criterion of the distribution of instincts. Given such a principle the author places Veblenian instincts within two groups: *a*) one group represented by those instincts that benefit the group – “group-regarding” instincts – and *b*) another one represented by those instincts that benefit the individual – “self-regarding instincts”. So according to the author, Veblen is interested in the meticulous study and characterization of the instinct of workmanship and the predatory instinct as the fundamental watershed between “group-regarding [instincts] and [...] self-regarding [instincts]” (Edgell, 2001, p.80; see also Ayres, 1958; Dugger, 1984; Edgell, 1975; Hunt, 1979; Tilman, 1996; Watkins, 1958). The classification presented by Edgell requires a clarification. He convincingly makes reference to group or individual in terms of benefit not necessarily in terms of aim. In other words the group-regarding instincts are compatible with self-interest but unlike self-regarding instincts they produce positive externalities for the collectivity.

On the other hand, O’Hara (1993, pp.111-112) makes reference to the parameter of *reproduction*. Given such a principle the author places instincts within two groups: *a*) one group represented by the instincts that intensify the reproduction of wealth of a community – “good” instincts and *b*) the instincts that control it – “bad” instincts. More in particular, the instinct of workmanship, the parental bent and idle curiosity are examples of good or group-regarding [instincts], while the predatory instinct, pecuniary instinct, salesmanship and pugnacity are examples of bad or self-regarding [instincts].

Seen in detail, the criteria used by Edgell and O’Hara can be conceived as homogeneous since the instincts that allow reproduction in fact are those that benefit the group and *vice versa* while the instincts that do not allow reproduction just benefit the single individual but not the society and *vice versa*. A further discriminating factor

can be traced in the element of *time*, by classifying instincts between farsighted and speculative, in other words between those which capitalize the present – like workmanship - and those that discount the future – like the predatory instinct. Let us see the Veblenian social classes and their instinct and institutions in more detail.

1.3.1 *The leisure class*

Veblen identifies the leisure class as the class whose components are excluded from industrial occupations since they have the right to “industrial exemption” (Veblen, 1975 [1899a], p.212). The right to industrial exemption is a consequence of their employment in other activities, mainly in those that are recognized as honorific and called “worthy employments” (Veblen, 1975 [1899a], p.1, p.8). It is important to point out that Veblen analyses the features of the leisure class – as well as of all social classes – starting from a clear distinction of labour into economic and non-economic employment. Economic employment is composed of “pecuniary employment” and “industrial employment” (see Veblen, 1975 [1899a], p.229); these two kinds of employment are economic since they are activities aimed at production of monetary or real income - even if “the aptitudes and habits of thought fostered by the one and the other class of employment [have] different economic value” (Veblen, 1899b, p.113) - while the non-economic employments include activities which are aimed neither at the production of income nor monetary or real income (see Veblen, 1961 [1901], pp.287-289). Industrial employment entails the material production of goods so it is considered productive labour, while pecuniary employment entails working activities whose aim is “make money, not to produce goods” (Veblen, 1964 [1919a], p.92) and for this reason it is considered – along with the non economic employments – as unproductive labour¹⁵. Veblen is particularly critical of non-productive occupations

¹⁵ The distinction between productive and unproductive labour is not new in literature. Classical economists agree on the distinction between the two kinds of labour. Adam Smith in chapter three of the second book of his “*An Inquiry into the Nature and Causes of the Wealth of Nations*” (1776) makes a distinction between productive and unproductive labour in terms of value and outcome. In the first case the labour of individual *X* is productive if it generates value in other words if individual *Y* is willing to transfer part of h/his own value-labour to *X* to obtain the value-labour of *X*. In the second case labour is productive when it is ‘storable’ in some material form. On the other hand labour is unproductive when it refers to those labours not ‘storable’ in material goods, that is to say those activities (services) that lose their serviceability as soon as they are supplied. John Stuart Mill in chapters two and three of the first book of his “*Principles of Political Economy*” (1848) also sustains Smith in his conception of productive labour intending it as labour able to produce real goods including – unlike Smith – the skills

since they are not essential for the society because they do not furnish material outcomes (see Veblen, 1899b, p.114). However even if they are not indispensable to the community they are “*integral features* of modern economic life” and consequently they must “be classed as *normal* [even if only] for the *existing situation*” (Veblen, 1961 [1901], p.287; italics added). In other words they are conventional activities – one could say *institutional* activities – even if non-productive in a strict sense, and for this reason non-indispensable¹⁶. As Veblen writes:

“There are activities and classes of persons which are unavoidably present in modern life and which draw some income from the aggregate product, at the same time that these activities are non patently productive of goods and can not well be classed as industrial” (Veblen, 1961 [1901], p.287).

Given the above considerations on productive/non productive labour, the leisure class can be said to be engaged in non productive labour. In addition the main feature of all activities of the leisure class is the exploitation which consists of “[...] the conversion to [the ends of an agent] of energies previously directed to some other end by another agent” (Veblen, 1975 [1899a], p.12)^{17,18}, or as he adds “it is [by] the exercise of

of workers and those services designed to increase skills. Moreover, Mill adds that the activities aimed at the protection of ownership must be considered productive activities. Marx instead in the first book of “*Capital*” (1867) considers productive labour simply the labor that produces surplus value. Instead Veblen seems to have a vision of productive labour in line with Smith and Mill in the sense that in his vision productive labour is the labour used to obtain real goods. In addition he considers labour employed in the pursuit of knowledge to be productive labour (see ch.2) but unlike Mill he does not regard services aimed at the support of ownership as productive labour (see ch.2). O’Hara (2000, p.73) – interpreting and expanding the Veblenian view – has identified a group of unproductive activities even if he does not assign such activities to a particular social class. He speaks about unproductive workers as “accountants, advertisers, public servants, members of parliament, owners of land and capital, banks and sales workers”.

¹⁶ Notice that several economists were interested to the study of the “social value” of the upper classes. Dugger (1998) has compared Karl Marx, Joseph Schumpeter and Thorstein Veblen on the issue pointing out that – unlike the others – Veblen appears to be extremely critical on the possibility that the behaviour of upper class can have positive effects on society. Differently from Veblen – Dugger stresses - the others recognize that the behaviour of the upper classes is functional for the society, even if “this is not to say that [Marx and Schumpeter agree that] the members of the upper classes intend to benefit society. They are not altruist. But that is to say they intend to benefit themselves and by doing so they also end up benefiting their society” (Dugger, 1998, p.74). So the aim of the construction of personal dynasties of entrepreneurs in Schumpeter and the aim of profits accumulation of capitalists in Marx can have a positive effect on society since they push the increase of innovation (Schumpeter) and improve several aspects of social and economic life (Marx) even if the Marxian functionality of the upper class has mainly a dialectic sense. In fact as Dugger (1998, p.75) adds – “the selfish pursuit of profits by the capitalists [in Marx] is leading, dialectically, to a destruction of capitalism itself”.

¹⁷ Historically he attributes the institution of the leisure class to the feudal period in which “the higher stages of the barbarian culture” predominated and in which the two main “honourable employments” were “warfare” and “priestly service” (Veblen, 1975 [1899a], p.1). Examples of members of the leisure class in Veblen are “[those that] may be roughly comprised under government, warfare, religious observances, and sports” (Veblen, 1975 [1899a], p.2)

control and coercion over the population [that the leisure class] draws its sustenance” (Veblen, 1975 [1899a], p.383). Members of the leisure class can refrain from productive labour thanks to some economic conditions and because of some institutional reasons. In the first case: *a*) members of the leisure class obtain *sufficient* income – mainly in the form of rent, *b*) their accumulation of wealth allows a subsequent or prior (to point *a*) above) abstention from productive labour. Instead, from the institutional point of view: *a*) “application to productive labour is a mark of poverty and subjection” (Veblen, 1975 [1899a], p.38), *b*) productive labour removes time from ostentation of “honorific waste” (Veblen, 1975 [1899a], p.116), that is to say, from the “method of demonstrat[ing] the possession of wealth” (Veblen, 1975 [1899a], p.85), in terms of time and possessions whose “expenditure does not serve human life or human well-being on the whole” (Veblen, 1975 [1899a], p.97). Not only does the leisure class own a great deal, but it also consumes a great deal. In fact it absorbs a large part of “[...] the net product of the country’s industry over cost” (Veblen, 1964 [1919a], p.163) just for ostentatious motives, which Veblen sees as futile, attributing “socially wasteful roles” (Tilman, 2003, p.xvi) to the leisure class.

It is important to notice that the recognition of worthy, unworthy, noble and ignoble is based on invidious judgement (see Veblen, 1975 [1899a], p.92). In these terms honourableness is a relative concept and is not innate to the nature of an act but rather to the social convention that gives this description of “a conventional basis of esteem” (Veblen 1975 [1899a], p.29). The conferring of honourableness can be seen therefore as an outcome of the mind. In this way a human act is honourable if it is actually or ideally emulated independently from any concrete evaluation on its utility, morality and modality of acquisition (see Veblen, 1975 [1899a], pp.15-21). Veblen sees envy, in particular, as a common motive for conferring honourableness to an act, thus leading people to emulate it (see Veblen, 1975 [1899a], p.26). On the honourableness of abstention from labour Veblen writes:

“Abstention from labour is not only a honorific or meritorious act [since members of the leisure class are engaged in other activities with higher value] but it presently comes to be a requisite of decency. [In addition] abstention from labour is the conventional evidence of wealth and is therefore the conventional mark of social standing” (Veblen, 1975 [1899a], p.41).

¹⁸ Since Veblen does not have a theory of value the term exploitation is not intended in Marxian terms. Exploitation – a term Veblen explicitly uses - means here the existence of “free income”, i.e. income which does not derive from productive activities, i.e. “unearned” (see Veblen, 1964 [1919a]).

Consequently highly honorific activities are the domain of the leisure class and such activities are different from working activities. In particular members of the leisure class can only perform “honorific”, “meritorious” and “decent” activities. Generally speaking the leisure class spends its time in “decorous employments” (Veblen, 1975 [1899a], p.115) that are not addressed to making a material product. Members of the leisure class direct their effort “on objects which are of no intrinsic use” which, in turn, take the form of “immaterial goods” (Veblen, 1975 [1899a], p.45). The improvement of these accomplishments is not functional to the production of real goods; instead it is instrumental for ostentatiously displaying the non-productive use of time. It is important to remark that “non productive use of time” is not equal to non-occupation; that is to say the leisure class is however a class that employs its time in some activity even if such activities are unproductive activities; in other words members of the leisure class are not employed in the direct production of real goods. So the leisure class is engaged in activities that correspond to three main requisites: *a*) they are immaterial and *b*) they do not have “intrinsic use”, *c*) they supply evidence of the leisure class’s ability to attach a different value and goal to effort compared to workers, i.e. they allow members of the leisure class to provide effort for *higher finalities* rather than for simply obtaining sustenance. The description of the “honourableness” of work given above enables us to look at the retributive gaps between social classes in different terms from the parameter of productivity or serviceability of work. It appears that the retributive system follows the logic of social recognition of the status of classes which are hierarchically ordered within the macroeconomic system (see ch.2).

There are several types of non productive consumption of time by the leisure class: *a*) the first kind is represented by pecuniary activities, *b*) the second one is represented by those activities aimed at the improvement and ostentation of *honourable knowledge*, in particular in “quasi-scholarly” or “quasi-artistic” knowledge (Veblen, 1975 [1899a], p.45)¹⁹, *c*) the third kind of non-productive consumption of time is represented by those activities of improvement and ostentation of *honourable gestural communication* – think for instance of the acquisition and ostentation of “manners and breeding, polite usage, decorum, and formal and ceremonial

¹⁹ On this point Veblen writes “for instance in our time there is the knowledge of the dead languages and the occult sciences; of correct spelling, of syntax and prosody; of the various forms of domestic music and other household arts; of the latest proprieties of dress, furniture, and equipage; of games, sports, and fancy-bred animals; such as dogs and race-horses” (Veblen, 1975 [1899a], p.45).

observances” (Veblen, 1975 [1899a], pp. 45-46); c) finally the third kind of non-productive consumption of time is engaged in the *training of tastes*²⁰. By the ostentation of ‘honourable knowledge’ the leisure class also has a significant role as controller of the education system. Veblen looks at the “educational system” as a system of discipline and control of individuals under the guidance of the leisure class. For Veblen education supplies a particular “economic value” for the upper classes: the “serviceability of the individual” (see Veblen, 1975 [1899a], p.363). The control of education expressed by the leisure class finds its origin in the “devotional function” of the earliest forms of education. As Veblen writes:

“In point of derivation and early development, learning is somewhat closely related to the devotional function of the community, particularly to the body of observances in which the service rendered the supernatural leisure class expresses itself. [It was] ”knowledge of ritual and ceremonial [and] what was learned was how to make oneself indispensable to [the supernatural leisure class]” (Veblen, 1975 [1899a], pp.364-365).

The leisure class’s capacity for controlling the education system is not absolute for Veblen since the leisure class can only control one kind of knowledge, namely what he calls “esoteric knowledge” or erudite knowledge – represented by “scholasticism and classicism” that is to say, knowledge with “no economic or industrial effect” and according to the author knowledge has an “economic or industrial effect” when it shows itself in “an articulate recognition of causal sequence in phenomena” (Veblen, 1975 [1899a], p.386). If knowledge is not scientific – that is to say when it is not based on “causal sequences” of phenomena – then the state of things is taken for granted by individuals. A spread of erudite knowledge serves the leisure class for the maintenance of the state of things since it does not form habits of thought addressed to a critical vision of reality. On the other hand, technological development has contributed to the spread of a different kind of knowledge, namely what he calls “exoteric knowledge”, that is to say “knowledge of industrial processes and of natural phenomena which were habitually turned to account for the material purposes of life” (Veblen, 1975 [1899a], pp.366-367). Such knowledge allows individual to know how a phenomena has been

²⁰ On this point Veblen remarks “in order to avoid stultification he must also cultivate his tastes, for it now becomes incumbent on him to discriminate with some nicety between the noble and the ignoble in consumable goods. He becomes a connoisseur in creditable viands of various degrees of merit, in manly beverages and trinkets, in seemly apparel and architecture, in weapons, games, dancers, and the narcotics” (Veblen, 1975 [1899a], p.74).

generated and how it can evolve, therefore providing tools of judgement on it and on its serviceability for the “material purposes of life”. In addition since Veblen stresses that the leisure class looks at the productive activity as a “mark of poverty and subjection” and therefore of social inferiority (Veblen, 1975 [1899a], p.38) then also each kind of “exoteric knowledge” becomes mark of inferiority. That is the reason why in the eyes of the leisure class “esoteric knowledge” is “higher learning” and “exoteric knowledge” is lower learning (see Veblen, 1975 [1899a], p.367). The interest of the leisure class in “esoteric knowledge” is in line with its proclivity to look at reality in terms of “belief” (cf. the instinct of workmanship) Members of the leisure class conform to an institution by psychological processes of adaptation rather than by forms of adaptation founded on facts. Consequently the psychological adaptation to the institution is for the leisure class the “belief in luck” (Veblen, 1975 [1899a], p.276) which represents “a sense of *fortuitous necessity* in the sequence of phenomena” (Veblen, 1975 [1899a], p.278; italics added). So members of the leisure class seem to believe in causality of progression of facts by two main forms: *a*) attributing the evolution of the fact to concrete and animated identities and objects – “quasi-personal character of facts” (Veblen, 1975 [1899a], p.279); *b*) attributing the evolution of the fact to abstract and no-animated identities – “preternatural agency” (Veblen, 1975 [1899a], p.280). The necessity of the above forms of belief is an institutional necessity, that is to say for acting as a predator the individual continually needs approval, recognition and support from high and authoritative real or abstract identities. So “the belief in luck” works as a precondition to predatory action; in other words if a predatory agent had not an optimistic expectation of the result of his/her action then s/he would not give concretisation to his/her predatory action.

The leisure class suffers institutional changes since these could threaten its privileged state. As Veblen writes:

“It is commonly the invidious one that the wealthy class opposes innovation because it has a vested interest, of an unworthy sort, in maintaining the present condition” (Veblen, 1975 [1899a], p.199).

On this point Cummings (1899, p.438) remarks that Veblen makes a mistake since he considers the leisure class contrary to *all* institutional changes. Contrary to Veblen, Cummings (1899, p.437) believes: “institutional inertia is not [...] inhibition of social progress and evolution but on the contrary is the very condition and *sine qua non* of

such progress". More specifically, Cummings's vision of social progress is equal to improvement of the present state of things so he stresses that social progress necessarily requires adjustment of institutions developed in the past and conserved in the present for the "accomplishment of human purposes" (Cummings, 1899, p.437). In opinion of Cummings (1899, p.437), Veblen regards institutional inertia as a form of inhibition of "all change, including progress itself". Actually – Cummings stresses – institutional inertia is against destruction of the present not against its improvement. In addition, in the view of Cummings (1899, p.437), the present institutions are the "evolutionary product of man's reaction upon his environment throughout those ages which have step by step developed man out of the ape [...] They are therefore worthy of conservation against innovation". Institutional inertia appears to be for Cummings a defensive tool of the cumulative state of development from past to present against the destructive perturbations of the quiet state that innovation could generate. Cummings remarks that it is obvious that the leisure class does not want to lose what it has. But at the same time it is also plausible to think that it wants to increase and improve what it has. On this point Cummings (1899, p.438) writes "the inertia of the leisure class is inertia against multifarious means of wealth dissipation". In addition he adds: "A railroad corporation has a material interest in preserving its railroad from destruction, in leaving it as it is, but the corporation has a greater material interest in making the railroad more efficient in service, and economical in management than it is. [So] *it is conservative against destruction, not against progress*" (Cummings, 1899, p.438; italics added). Cummings's interpretation can be configured – according to Forges Davanzati (2006a, p.65) – as "institutional change without economic growth". In other words it is reasonable to think that the leisure class is not opposed to progress and consequently also to all institutional changes, but in Veblen institutional changes are those that assure social well-being – "institutional change with economic growth" – not those that improve the living conditions of the leisure class: that is the sense of "innovation" in Veblen; the conservative action of the leisure class is therefore addressed to preserving things from "innovations" so its action is addressed to maintaining institutional inertia and therefore social inertia (see also Edgell, 2001, p.13).

1.3.1.1 *Instincts and habits of thought of the leisure class*

The emergence of a leisure class calls for a particular kind of activity: exploitation. So the emergence of the leisure class requires the identification of the socio-economic conditions for the origin of exploitation, as well as for the origin of the class which has the right to enjoy the exploitation itself. In the first case Veblen thinks about the following two main conditions: *a*) a predatory habit of life, that is to say the “infliction of injury by force and stratagem” (Veblen, 1975 [1899a], p.8) and *b*) the social production of surplus²¹. With particular reference to the surplus it is important to notice that Veblen defines surplus – or net production or profit – as “the amount by which the actual production exceeds its own cost, as counted in terms of subsistence, and including the cost of necessary mechanical equipment” (Veblen, 1964 [1919a], p.55)²². In addition he writes:

“The conditions [...] necessary to [the emergence of exploitation] are: (1) the community must be of a predatory habit of life. [...] That is to say, the men, who constitute the inchoate leisure class [...] must be habituated to the *infliction of injury by force and stratagem*; (2) subsistence must be obtainable on sufficiently easy terms to admit of the exemption of a considerable portion of the community from steady application to a routine of labour” (Veblen, 1975 [1899a], p.8; italics added).

In the second case instead “the emergence of the leisure class coincides with the beginning of ownership [...] as a conventional right or equitable claim [...] to extraneous things” (Veblen, 1975 [1899a], p.22-23; italics added; see also Veblen, 1898b), including not only material things but also “personal services” directly supplied by others –think for instance of the role of “servants”, women, etc. (see Veblen, 1975 [1899a], pp. 53 and ff.). As a result, the “habitual appropriation” of things generates ownership of the same when: *a*) things are produced by individuals who are different from the holders and *b*) the right to the possession is conventional, not natural.

More specifically, the concept of natural ownership is expressed by Veblen thus “[...] the person who has *produced* an article or [...] by a constructively *equivalent*

²¹ As Veblen remarks “a predatory life is possible only after the use of tools has developed so far as to leave a large surplus of product over what is required for the sustenance of the producers” (Veblen, 1898a, p.194).

²² Gruchy (1958, p.12) remarks that – with the exploitation/surplus relationship - “Veblen’s object is to show that some of the consumption component of total output constitutes a surplus or net product, which goes to [the leisure class rather] than to the working population”.

expenditure of productive force has found and appropriated an object [has the natural right to possess it]" (Veblen, 1898b, p.353; italics added). Natural ownership therefore has a strict economic relevance. Its naturalness is inborn in the origin of this kind of property. Natural ownership is always linked to the outcome of a productive activity. So the productive effort supplied is the reason for its existence. It could be argued that natural ownership is the natural legitimation of material possession aimed at the absolute private pleasure proportionate to the grievousness of the productive effort supplied. Consequently, in a system characterized by natural ownership the exchange of ownership is natural since it refers to real goods and it is fair since nobody has more goods than what s/he has helped to produce.

In contrast, there is nothing natural in the *current* sense of ownership. It is simply a conventional attribution of the right to other things. This right was born as a prerogative of the leisure class since possession of things allows a concrete exhibition of "some durable result of [...] exploits" (Veblen, 1975 [1899a], p.24). As Diggins (1977, p. 119) remarks "Veblen perceived the [...] institution [of ownership as] the act of conquest [and seizure]"; so it could be argued that the higher the "force and stratagem" used for the appropriation of things, the higher the image of its "prowess". More specifically, the logic of the existence of ownership can be found in three particular elements:

"(1) A propensity for dominance and coercion; (2) the utility of [owned things] as evidence of the prowess of [the] owner; (3) the utility of their services" (Veblen, 1975 [1899a], p.53).

So ownership represents a conventional tangible indicator of social "prowess" recognized as honorific "prowess", where the dignity of the leisure class is assured by a widespread proclivity to emulation (see Veblen, 1975 [1899a], pp.15-21). It is interesting to notice that the right to own does not entail a duty to supply. In other words the *right to have* does not have a 'meritocratic' nature, in fact "force and stratagem" requires proclivities such as astuteness rather than proclivities to efficient effort. On this point Veblen remarks "the possession of wealth which was at the outset valued simply as an evidence of efficiency, becomes, in popular apprehension, itself a meritorious act" (Veblen, 1975 [1899a], p.29).

In view of the above, the leisure class can exist and act if society produces surplus and if this surplus is mainly distributed in favour of the same class. So the

production of surplus is the condition for the existence of the predatory instinct just as the predatory instinct is the condition for the existence of an unfair system of income distribution²³. In addition, as we shall show more clearly below, the production of surplus requires the existence of a particular instinct: the instinct of workmanship. Even though Veblen is not clear on this point, one could argue that the first instinct characterizing the evolution of the human species must have been the instinct of workmanship, and this also means that the instinct of workmanship was the instinct from which the others were generated. What is more, if the institution linked to the predatory instinct is ownership while the institution linked to the instinct of workmanship is industry - “the effort that goes to create a new thing” (Veblen, 1975 [1899a], p.12) - then it was industry that gave rise to ownership. So while the production of a surplus is strictly linked to the instinct of workmanship and the institution of industry, the distribution of income is strictly linked to the predatory instinct and the institution of ownership.

Hence, amongst the other features of the leisure class there are three particular characteristics to consider: the leisure class owns a great deal, consumes a great deal and does not produce real goods. Its wealth consists of different kinds of goods: land, money, real estate, stocks, bonds, precious metals, etc. Veblen does not see such goods in terms of savings; in fact the traits of leisure class consumption leave no space for savings; its income is therefore prevalently used for consumption. However at the same time the leisure class holds wealth, but what does such wealth depend on? The traits of the leisure class provide the answer to this question; in other words the wealth owned by the leisure class is historically acquired by activities of predation and the exploitation of the right of ownership. Amongst the kinds of goods owned in the form of wealth, a particular role is played by money, stocks and bonds. In fact – and this will be shown better below – Veblen looks at money in terms of the initial and final goods on which the production circuit depends, and anticipating the description of this circuit money (see ch.2) – with which the system starts production – is therefore mainly in the hands of the leisure class, which in fact has the right to the production of money, a right – it could be argued – historically obtained. The leisure class supplies money to the system for production since production serves for its consumption. Money is supplied to the production system in two forms: *a*) by loans to undertakers,

²³ The meaning of a perception of an unfair income distribution in a Veblenian perspective will be better investigated in the chapter 3.

b) by acquisition of stocks; in the first case the leisure class is the financier of firms, in the second case it is financier-capitalist of firms²⁴.

1.3.2 *Undertakers*

undertakers are the capitalists and/or the managers of firms. The trait of the undertaker as capitalist and/or manager depends on the role of the leisure class in the production system. In particular when members of the leisure class buy stocks then undertakers become mere managers while the role of capitalists is attributed to the leisure class. On the other hand, when the leisure class supplies money as loans to undertakers then the leisure class is merely the financier of firms and the undertakers become capitalists and managers. In this last case Veblen assumes that undertakers – like the leisure class – can hold money, and such money is the outcome of the accumulation of past profits. Apart from the formal figure of capitalists or managers, undertakers are materially involved in the conduct of firms for business purposes, in other words to make monetary profits. Veblen generally recognizes profit as “the amount by which the actual production exceeds its own cost, as counted in terms of subsistence, and including the cost of necessary mechanical equipment” (Veblen, 1964 [1919a], p.55). The undertakers’ aim is to obtain monetary profits since they have an aptitude for the business side of management of firms (see Veblen, 1964 [1919a], p.91); an interesting issue is to understand if firms are interested in a maximum level of profit or in a normal one. In his works Veblen changes his view on this point originally stressing the aim of normal profits, then moving onto the maximization of profits and competitive advantages. The idea of profit maximization is clear in the following quotations which will be considered again for other purposes:

“Profitable sales can be made only if prices are maintained at a profitable level, and prices can be maintained only if the volume of marketable output is kept within reasonable limits [where] reasonable means what the traffic will bear, that is to say what will yield the largest net return”

²⁴ It is important to notice that in Veblen there is also an idea of production of money by the banking system alongside the holding of money by the leisure class. As the author writes “broadly speaking” [...] “banking is profitable chiefly because the banker lends more than that he has or borrows”, and “the banker [can] create a new volume of credit” (Veblen, 1905, p.470).

(Veblen, 1964 [1919a], p.91 italics added; see also Veblen, 1904, ch. 3 and ch. 5; Veblen, 2001 [1921], p.66).

He also writes:

“The earning-capacity [of capital] is determined by what the traffic will bear, that is to say by curtailing production to such an amount that the output multiplied by the price per unit will yield the largest net aggregate return” (Veblen, 1967 [1923], p.68).

On the other hand, on normal profits Veblen remarks that this is assumed as the “natural thing” for undertakers; it is based on undertakers’ common sense in looking at business. Veblen does not spend much time explaining the meaning of normal profit; as he remarks normal profit can mean average net return or “something else”. In other words normal profit is just a matter of undertakers and profit is normal when undertakers are clear as to its sense, entity and stability so they spend their time thinking over “the businesses” (see Veblen, 1904, ch. 4). Veblen tries to clarify the question of normal profit by stating that it is concretely the profit on whose level undertakers are willing to employ their own capital in the firm’s activity (see Veblen, 1904, ch. 4). In addition he stresses the uselessness of an exact definition of normal profit; in fact on this point he writes:

“The precise meaning of "ordinary profits" need not detain the argument. It may mean net average profits, or it may mean something else. The phrase is sufficiently intelligible to the business community to permit the business men to use it without definition and to rest their reasoning about business affairs on it as a secure and stable concept; and it is this commonplace resort to the term that is the point of interest here” (Veblen, 1904, p.87).

Since undertakers are only interested in business matters they remove themselves from industrial management and production of firms, delegating this activity to “practical [...] men [...] who are possessed of [...] workmanship ability” (Veblen, 1975 [1899a], p.230). As he writes: the undertakers is mainly an “economic manager” – not a technical manager – of industry (see Veblen, 1975 [1899a], p.230), so undertakers are interested in production for making money and not for satisfying human needs and welfare (see Veblen, 1961 [1901], pp.303-304). In other words – see in detail chapter 2 – undertakers are interested in monetary profits via the ‘monopolization’ of markets addressed to reducing quantities of production so as to increase prices. The undertaker

deals with commercial and financial transactions, with “distribution and circulation of goods” (Veblen, 1961 [1901], p.27) and with credit operations. So undertakers deal with “the phenomena of *value*”, with “exchange or market values”, with “purchase and sale”; so they “sell in order to buy cheaper [and] buy in order to sell dearer” (see Veblen, 1961 [1901], p.293; p.296-297). As Veblen stresses:

“These activities begin and end within what may broadly be called the higgling of the market” (Veblen, 1961 [1901], p.294).

Being interested in the “higgling of the market” the undertaker just acts by evaluating the results of her/his actions in terms of influencing and persuading in the phase of exchanges (see Veblen, 1961 [1901], p.294). An increase or decrease of exchange values can affect the aggregate production mainly in terms of “serviceability” of goods to produce, and indirectly its quantity and quality. In pecuniary terms a good is “serviceable” if it is vendible and all judgements on its utility in terms of “human welfare” are excluded (Veblen, 1961 [1901], p.304).

In addition, the undertaker’s activity is competitive. Veblen sees competitiveness as a game based on improvement of methods of selling outcomes and on the introduction of new technology. In fact such competition is based on the pecuniary excellence which appears to be a *struggle* for simple ownership; someone obtains something if s/he wins the competition thus preventing the other from the possibility of reaching the same result. In other words the Veblenian competition is configurable as positional competition by which each firm acts on the market with the aim of obtaining competitive advantages over others. The removal of a competitor from the struggle is mainly based on the capacity to obtain higher monetary gains. So the possibility of having higher pecuniary gains depends on the ability to exchange, and ability to exchange requires the ability to increase the value of the things exchanged; it is not important to increase the real value of these things but their exchange value, acting, if needed, by fraudulent practices so as to create a large gap between the exchange value and the effective value. So - even though Veblen does not directly highlight this point – undertakers act following proclivities that are recognized as honorific if they provide “success and superior force” (Veblen, 1975 [1899a], p.181). undertakers therefore act through the institution of ownership and attitudes of

“salesmanship”, “bargaining”, “effrontery” and “make-believe” which are all similar aspects to the predatory instinct (see Veblen, 1967 [1923], p.78, p.108).

1.3.3 *The instinct of workmanship*

Unlike the leisure class and undertakers, technicians are engaged in industrial occupations. As Veblen remarks “[these activities] begin and end *outside* the higgling of the market” (Veblen, 1961 [1901], p.294; italics added), in other words they are employed in the industrial sector and they must deal with mechanical processes. Technicians are interested in continually improving the industrial process and in increasing production. They act and evaluate the efficiency of their own activity in terms of “mechanical effects” on the production process (see Veblen, 1961 [1901], p.294). So they aim to continually innovate and supply useful effort, i.e. effort that serves to create new things (see Veblen, 1975 [1899a], p.12). Let us see their instincts and institution in greater detail.

A) *The instinct of workmanship and the institution of industry.* Veblen’s instinct of workmanship can be interpreted in a double manner: a) as a primary instinct, and b) as a ‘current’ trait of technicians.

a) *Workmanship as primary instinct.* Veblen builds his theory of the workmanship instinct with the purpose of making a critique of the neoclassical theory of labour supply. In particular he wants to critically reply to the neoclassical axiom of labour disutility which is summarised by the same author in the following terms:

“It is one of the commonplaces of the received economic theory that work is irksome. Many a discussion proceeds on this axiom that [...] men desire above all things to get the goods produced by labor and to avoid the labor by which the goods are produced” (Veblen, 1898a, p.187).

Veblen summarizes the above axiom stressing that neoclassical economics agrees on the idea that any form of working effort is useless in the sense that working activity only supplies disutility and painfulness, leading individuals to prefer different activities. Veblen opposes this generalization since in his vision the human being can be characterized by natural traits that positively direct the individual toward her/his labour activity. So for Veblen disutility is an irrelevant concept for a theory of labour

supply. However apart from this critique Veblen in fact does not present an alternative theory of labour supply. Interpreting the sense of workmanship John Maurice Clark (1960 [1948], pp.56-57) critically replies to Veblen arguing that efficiency can only be attributed to “work” not to the worker. In other words, the author points out that the instinct of workmanship cannot be a human trait, it is a consequence of the characteristics of work. More specifically, the attitude to efficient work is connected to the nature of the work itself and not to the nature of workers. Consequently it is simply a matter of technical efficiency. So only technology can positively direct workers towards labour activity and not *vice versa*. The axiom of disutility therefore has its validity and it is only technological development that can mitigate the disutility. According to Veblen (1899a; 1922 [1914]) in the primitive phase of human evolution individuals did not try to avoid work since this was not possible in the sense that it was in the nature of things; individuals were *naturally* called to continually supply “useful effort” that is to say any form of material contribution to the production of everything -“the material means of life” (Veblen, 1922 [1914], p.39) - that was strictly needed and vital for survival and development (see Veblen, 1898a, p.187). As a result, individuals had a natural predisposition to work that is to say an instinctual “proclivity for taking pains” (Veblen, 1922 [1914], p.33). This natural and instinctual proclivity supplied utility to the individual in the sense that it assured the material production of those tools that were needed to overcome the adversities imposed by the process of natural selection. Veblen calls this natural, and therefore, instinctive human proclivity the *instinct of workmanship* (Veblen, 1898a, p.189). Workmanship is the instinct to be efficient and to supply “industrial effort” where “any effort is to be accounted industrial only in so far as its ultimate purpose is the utilisation of non-human things” (Veblen, 1975 [1899a], p.10)²⁵. Due to a natural constraint, therefore the natural instinct to ensure survival, individuals supplied their own services in industrious activities (see Veblen, 1922 [1914], pp. 31-32). Without an inborn attitude to the allocation of working services in this particular kind of activity, the individual would not have had those tools needed for her/his survival and evolution in a generally adverse environment. In addition, the absence of the instinct of workmanship would have required the presence of a friendly environment where natural selection would

²⁵ As has been said above, Veblen sees industry as “effort that goes to create a new thing, with a new purpose given it by the fashioning hand of its maker out of passive (“brute”) material” (Veblen, 1975 [1899a], p.12).

not have had no influence on human development. But since, as the same author remarks, the world is not an Eden - because “the trial of the Edenic serpent [does not] plain to all men” (Veblen, 1898a, p.187) - individuals realistically do not have freedom to choose whether to work or not and their own preferences cannot play a major role in individual decisions. The selection process requires an active and continued – therefore industrious – effort which is addressed to the maintenance and evolution of the human species (see Veblen, 1898a, p.187). The above description allows us to interpret Veblen in the following terms: the instinct of workmanship is the primary instinct since the human species started its evolution thanks to a common instinct, i.e. the instinct of workmanship. Since the instinct of workmanship was a common feature of all individuals and since they habitually acted in order to produce material goods, they acquired a particular kind of institution: the institution of industry. However thanks to the progress of knowledge and skills the community started to produce more than was strictly necessary to its survival. So the production of a surplus due to technological progress allowed some to remove themselves from the productive process since their presence was no longer necessary. Obviously their non-productive utility had to be provided by other kinds of ‘utilities’ for the community and this research was necessary to avoid social exclusion. So the community found additional kinds of not strictly productive activities – war for example – which were however instrumental in increasing the social surplus and consequently instrumental for the development of the community itself. At the same time, the community found additional utility in the cure of children and the research of knowledge. In view of what has been said, workmanship appears to be the source of the other instincts, so the source of the related institutions and so of social differentiation. However, apart from the primary process of evolution, social development continues thanks to the co-presence of industrial activity and non-industrial activity, in other words allowing the co-presence of the instinct of workmanship and other instincts, i.e. the co-presence of the institution of industry with other institutions. On this point Shannon (1996, p.5) remarks “Veblen offers not so much a history of the instinct of workmanship but rather history as the instinct of workmanship”.

b) Workmanship as ‘current’ trait of technicians. The Veblenian study of the instinct of workmanship as the current trait of technicians is strongly influenced by the historical circumstances of his times. As remarked by Edgell (2001, p.4) Veblen lived

in a time of great change in the United States; in fact, the author writes “at the beginning of Veblen’s life, America was a predominantly agricultural society. [...] By the end of his life an expanded and politically unified America had displaced Britain as the world’s leading industrial nation, and had inaugurated the era of mass production and consumption”. Historians – see for example Cameron (1993, ch.9-12) – in fact recognize the United States as an extraordinary example of the rapid economic growth of the 1800s. According to the author the population was about forty million in 1870 and about a hundred million in 1915; such an increase was both the result of European immigration and also of internal development; one element that helped the population increase was the increase in wages due to the scarcity of the labour force compared to the availability of land and to other resources. Cameron argues that there are two main reasons for the rapid growth of the United States: *a*) technological development, *b*) regional specialization where the use of industrial equipment was strongly stimulated by the high cost of labour. Moreover, the expanse of the United States – combined with the differentiation of climate and of resources – led the Nation to a strong regional differentiation of production. These combined aspects allowed both industry and agriculture to be constantly involved in technological innovations, along with the fact that they were always oriented to the market. As a result, the nation saw the development and spread of industrial activities and of industrial employment on the one hand and the spread and development of business activities and of business employment on the other. The consequence of the parallel development of industrial and business employment was the development of two parallel classes: the class of technicians and the class of businessmen, where only the first class is assumed indispensable for the collectivity. As Veblen states:

“The technicians are indispensable to productive industry of this mechanical sort; [...] it follows that the material welfare of all the advanced industrial peoples rests in the hands of these technicians” (Veblen, 2001 [1921], p.84).

Differently from point *a*), here Veblen intends to investigate the instinct of workmanship as the trait of the new emerging social class: technicians (see also Edgell, 2001, ch.7). Following this line Veblen identifies three interdependent aspects of workmanship: *a*) creativity, *b*) proficiency and *c*) “[the] technological mastery of facts” (Veblen, 1922 [1914], p.33). Creativity and proficiency are variables of

workmanship on which Veblen places little emphasis and they are not generally examined by the literature, while “the technological mastery of facts” is the main matter of investigation. With particular reference to this point it is possible to say that in Veblen’s view, facts prevail on the technological plane because they govern both culture and technique. So to Veblen’s mind, technology is a broad concept. In fact he does not limit technology to the mere mechanical and technical plane: it is first of all a matter of mental disposition to reasoning on evidence and facts. The central point on which technology depends is the current state of matter of fact logic rather than the materialistic state of things. So technology is first of all a mental matter and then a material matter. But if technology is a variable of workmanship and technology is a mental matter, then workmanship is a mental and therefore a human trait (cf. John Maurice Clark (1960 [1948], pp.56-57). In these terms “the logic of workmanship” is mainly a “matter of fact[s]” and “matter of imputation” by which each event is observed in terms of evidence and “objective knowledge” (Veblen, 1922 [1914], p.55-56). Such logic allows people to explain facts in terms of cause and effect. A logic working on this plane is able to structure the cultural patrimony and the general life of a collectivity in terms of realism, scepticism and materialism (see Veblen, 1904, ch. 9). Consequently, individuals are pushed to apprehend facts for what they objectively are (*imputation*) or for what they will objectively become (*derivation*). Veblen comments thus:

“In the workmanlike apprehension [...] the nature of things is twofold: a) what can be done with them as raw material for use under the creative hand of the workman who makes things, and b) what they will do as entities acting in their own right and working out their own ends” (Veblen, 1922 [1914], p.54).

If facts are interpreted by the above method then the instinct of workmanship forms an aptitude for change, for the evolution of thought and knowledge; consequently, this method of interpretation of facts can be considered to be at the basis of *reformist attitudes* (see ch. 3; see also Veblen, 1904, ch.9).

B) Idle curiosity. Veblen looks at “idle curiosity” as “desire for knowledge” (Anderson, 1933, p.603). Veblen writes:

“Idle curiosity formulates its response to stimulus, not in terms of an expedient line of conduct, nor even necessarily in a chain of motor activity, but in terms of the sequence of activities going on in the observed phenomena” (Veblen, 1961 [1906a], p.7).

In the presence of idle curiosity the observed phenomenon becomes the centre on which the individual focuses his/her attention. In particular the observed phenomena are not studied for a particular purpose; in other words they do not serve either individualistic or altruistic aims. The expedient line of conduct recalls the idea of action driven by the predatory instinct, the main self-interest instinct, while the chain of motor activity recalls the idea of matter-of-fact so of the instinct of workmanship, which is in fact an altruistic instinct at least in its effects and not in its purposes. On the other hand, in idle curiosity the cause of action is the knowledge of the observed phenomena and the effect of the same action continues to be the knowledge of the same observed phenomena. In this way the desire for knowledge becomes desire to provide answers to the phenomena as if the questions were raised by the phenomena themselves and not by the individual. Walker (1977, p.220) writes: “[Veblen] did not mean that the curiosity is idle or aimless, but that it operates only if there is surplus energy after the satisfaction of essential needs; and meant that humanity is motivated by a desire to discover knowledge independently of the desire for material gain and of any utilitarian aim”. It might be wrongly thought that Veblen looks at idle curiosity in terms of knowledge that is non-serviceable for the well-being of the collectivity. In view of the above, Veblen seems to emphasize the role of workmanship rather than idle curiosity for the well-being of society, but this does not mean idle curiosity does not positively affect social well-being since workmanship can be seen as an outcome of idle curiosity. In other words instincts are also overlapping (see Asso and Fiorito, 2004). This is the particular interpretative line of the institutionalist economist Lawrence Kelso Frank (in Asso and Fiorito, 2004, p. 564) who in the 1920s wrote: “scientific and technological effort [...] has to wait for the emancipation of human intelligence from animistic belief and practices”. In fact in the long run idle curiosity entails a practical serviceability for society since a feature of gaining knowledge for the sake of knowledge is its systematisation. In other words vague answers in a quest for knowledge become certainties, and these same certainties will be selected for application to the needs of the human species (see Veblen 1922 [1914], p.87).

1.3.4 Workers

Workers are the component of society engaged in industrial activity but unlike technicians “they supplement the machine process rather than make use of it” (Veblen, 1922 [1914], p.307). Workers are economically dependent on undertakers and technically dependent on technicians so they mainly present a servile instinct that is functional to survival. As Walker (1977, p.230) writes, workers are the “amorphous, passive, and anonymous mass”. Workers represent the “people” (Veblen, 1899, p.187), the “inferior class” (Veblen, 1975 [1899a], p.8), “common men” (Veblen, 1975 [1899a], p.8), the “underlying population” (Veblen, 2001 [1921], p.72). Veblen identifies workers as “common men” for two main reasons: *a*) they work to earn a livelihood rather than acting to “get something for nothing” – like the upper classes, *b*) they are numerous in the community (see Veblen, 1964 [1919a], p.162).

The inferior class takes a negative view of its own working activity, considering it irksome. Members of this class are inclined to consider their working activity as a source of useless effort. Unlike other classes, for the inferior class working activity is just a necessity and source of disutility. So workers highlight “[a] conventional antipathy to work” (Veblen, 1898a, p.190) unlike technicians who see their own work as a tool for the improvement of knowledge and skills, and unlike the leisure class that is in fact engaged not in working activities, but mainly in other more *honorific* activities - that is to say highly profitable activities which do not call for a particular physical or mental effort. As Veblen remarks:

“With more or less sincerity, people currently avow an aversion to useful effort. The avowal does not cover all effort, but only such as is of some use; it is, more particularly, such effort as is vulgarly recognized to be useful labor” (Veblen, 1899, p.187).

So it falls to workers to carry out those exhausting, modest, “unworthy” (Veblen, 1975 [1899a], p.8) even if indispensable activities for the collectivity; workers’ activity has to do “directly with the everyday work of getting a livelihood” (Veblen, 1975 [1899a], p.2). Moreover the allocation of workers to the productive sectors depends directly on the choices and behaviour of the upper classes about what must be produced and in what quantity. Workers are the identifiable “impecunious class” (Veblen, 1975 [1899a], p.26) since they consume the whole of the income received for their activity.

Veblen does not spend much time on the analysis of the instincts and habits of thought of workers. He in fact attributes the instinct to the struggle for subsistence to them as well as a conservative – passive and docile – habit of thought. On this point in fact Veblen remarks:

“The objectively poor and all those persons whose energies are entirely absorbed by the *struggle for daily sustenance* are *conservative* because they cannot afford the effort of taking thought for the day after to-morrow” (Veblen, 1975 [1899a], pp.203-204; italics added).

Note that the conservative habit of thought of workers is a consequence of low levels of subsistence. The lower the subsistence the lower the workers’ critical attitude of thought since if the subsistence is low workers only have energies for surviving. In fact even if the consequence of the passivity of the underlying population is low-level subsistence Veblen does not attribute an economic nature to this passivity, in the sense that the underlying population are not passive because there is some hypothetical benefit greater than the hypothetical cost of passivity. He instead attributes a metaphysical motive to the underlying population’s passivity. As he writes:

“There is a *naive, unquestioning* persuasion abroad among the body of the people to the effect that, *in some occult way*, the material interests of the populace coincide with the pecuniary interests of those business men [...]. This persuasion is an *article of popular metaphysics*, in that it rests on an *uncritically* assumed solidarity of interests, rather than on an insight into the relation of business enterprise to the material welfare of those classes who are not primarily business men” (Veblen, 1904, pp.286-287; italics added).

Veblen adds that the primary principles of the metaphysical nature of the passivity of the underlying population are “patriotism and property” (Veblen, 1904, p.288) that are ruled by irrational motives: the “unreasoning sentiments”. As he remarks:

“The substance of both is of the nature of *unreasoning sentiment*, in the sense that both are insisted on as a matter of course, as *self-legitimizing grounds of action* which, it is felt, not only give expedient rules of conduct, but *admit of no question* as to *their ulterior consequences or their value for the life-purposes of the community*” (Veblen, 1904, p.288; italics added)²⁶.

²⁶ On this point Tsuru (1993) has written: “Veblen [...] differs from Marx and Engels in thinking that the state does not exclude the underlying population from the governing process for the reason that the business leadership would not be able to govern without ‘the advice and consent of the common run’

Even if the passivity of the underlying population is a fact for Veblen based on irrational motives, in chapter 3 it will be argued how and under what circumstances the underlying population stops being passive. More specifically it will be argued how “unreasoning sentiments” push the underlying population into conflict with the upper classes when the real income is not in line with the subsistence wage.

1.3.5 *Instincts common to the social classes*

In view of what has been said, the institutional foundation of predatory instinct is ownership. According to Diggins (1977, p.123) this can give rise to an interesting question: “if property is founded upon conquest and seizure, must we conclude that man is aggressive and acquisitive?” As the same author remarks, some Veblenian instincts contain “the *potential* for contributing to the material welfare of the community” (Diggins, 1977, p.123; italics added) even though Veblen is not able to furnish an exhaustive explanation on their origins; Veblen in fact considers these altruistic attitudes as “unfolding impulsive activit[ies]” (Veblen, 1975 [1899a], p.15) and more specifically he identifies three kinds of non-predatory instincts: *a*) the instinct of workmanship, *b*) the parental bent, and *c*) the instinct of solidarity and sympathy. The term potential is not used lightly by Diggins. In particular the author – interpreting Veblen – assumes such instincts as potential since their concrete form is mitigated by their propensity to corruptibility. As he writes “the instinct of workmanship can combine with a concern for beauty to produce goods which are both useful and aesthetic [...]. The parental bent *is no less corruptible*. It may have its origins in altruistic impulses, but it gives way to the ‘self-regarding sentiment’ of a ‘gerontocracy’ as subservience to able-bodied elders gains the upper hand in the increasingly predatory [...] culture” (Diggins, 1977, p.125; italics added). So Diggins seems to attribute an explicit intention – in Veblen - to describe the institutional development in regressive terms since such development is identified as cause of the process of corruption of the above and named as “innocent institutions” by him. In

[...] Veblen was aware of a possible crisis [and] he developed a theory regarding the counter instruments to which the business leadership was expected to resort. Thus came his theory of ‘national integrity’ (or plain nationalism) into the picture. It had two aspects, namely: (1) equating the interests of business leadership with those of the nation as a whole; and (2) adopting aggressive policies towards the outside world, accompanied by the militarization of society”.

describing an evolutive process in regressive terms Diggins indirectly sees Veblen moving away from the strong, 'positivistic' Darwinian vision of selection. As Diggins writes with reference to Veblen "he could not accept the position of [...] Social Darwinists, who looked to the principle of natural selection as evidence that man is naturally combative and socially competitive". In fact, in that "could not accept" Diggins shrewdly looks at the origin of Veblen's normative position.

Parental bent and the instinct of solidarity and sympathy denote an altruistic proclivity in the individual. They reveal aptitude for the well-being of other individuals on the part of the agent. The formal difference is that while the parental bent is the specific attitude to the well-being of family and descendants (see Veblen, 1922 [1914], p.48) the instinct of solidarity and sympathy is the specific attitude to "charity, [to] social good-fellowship, or conviviality" (Veblen, 1975 [1899a], p.333) that is, to the welfare of non-parental individuals or groups. So both the instincts are attitudes to the well-being of others and it is possible to increase others' well-being if there is also an increase in efficiency. This is why Walker (1977, p.220) argues "[parental bent] reinforces the instinct of workmanship in the pursuit of efficiency".

1.4 Structural conflicts and unemployment

In Veblen the life of social classes is characterised by a continuous conflict, conflict that finds its origin in institutional motives. More specifically, Veblen stresses that while the working class fights for subsistence, undertakers fight for wealth and the leisure class for excellence. So Veblen identifies three possible causes of conflict: *a)* the "struggle for subsistence", *b)* the "struggle for wealth" and *c)* the "struggle to excel" (see Veblen, 1975 [1899a], p.24). In fact subsistence, wealth and excellence are institutional causes of action – causes driven by habits of thought – of the social classes aiming at the possession of goods, but since the effects of these actions may diverge from the goals then the social classes may come into conflict with others that have hampered – or are thought to have hampered – the reaching of the goal. The above causes of actions and conflict are therefore all pooled into one goal: the possession of goods, i.e. the institution of ownership. As Veblen writes:

“Wherever the institution of private property is found, even in a slightly developed form, the economic process bears the character of a struggle between men for the possession of goods” (Veblen 1975 [1899a], p.24).

On the whole the literature agrees on the interpretation of conflict in Veblen even if it limits its analysis to the macro plane. In other words it is generally recognized that the Veblenian conflict is a conflict of institutions for itself or a conflict of institutions in the distribution of wealth. More specifically the conflict of institutions derives from the “division of interest[s] between the business community, who do business for the [business purposes], and the underlying population, who work for a living” (Veblen 2001 [1921], p.67) and who in fact “suffer the inconvenience of it all” (Veblen, 2001 [1921], p.72). Anderson (1933, pp.620-621; see also Harris, 1951; 1953) for example remarks: “Veblen [fundamentally] conceives the [major economic] problem to be that of constructing that set of institutions most effective in *overcoming* scarcity²⁷. Harris (1951, p.68) adds that “in the struggle for existence [...] instincts [...] become organized into social habits, but the extent to which any one of them enters into the composition of habits is a matter of selective adaptation induced by changes in the material conditions of life”. The conflictualistic nature of Veblen’s vision is also emphasised by Edgell (1975, p.276) who in describing Veblen’s machine era (see ch.3) writes: “The climax of Veblen’s contribution was a concern to understand the social, economic and political ramifications of the negation of workmanship during the machine era that he attributed to the conflict between habits and institutions of business and industry”. In addition Edgell adds (2001 pp.5-6) that Veblen’s contraposition of industry and business probably finds its inspiration in the radical-populist movement of the 1890s which was engaged in a political conflict for the defence of farmers and “small-scale capitalism” against the increase of “monopolistic industrial capitalism”²⁸. Moreover as Walker (1977, p.235) writes: “[Veblen] applied his theory to the special case of change under capitalism, portraying a conflict between the institutions of the system of natural rights and the institutions that result from the impact of the modern machine

²⁷ “While [neoclassical economists] conceive[...] the economic problem to be one of making the best use of the resources already at hand within the existing framework of institutions” (Anderson, 1933, pp.620-621).

²⁸ Veblen did not only make critiques on the spread of business culture in strictly productive sectors. Also relevant is his critique of the spread of business culture into the education sector. As Edgell (2001, p.21; italics added) stresses “the thrust of Veblen’s critical study was that businessmen, their priorities and their culture were increasingly dominating and contaminating American institutions of higher learning, *to the detriment of the disinterested growth of knowledge*”.

process”. Tilman (2003, pp.xv-xvi) has recently argued that “Veblen’s theory is powerfully dualistic” and that this dualism is evident in all such occasions in which Veblen argues his case in a conflictual manner, using expressions such as “struggle between animistic and the matter-of fact”, [...] “between business and industry”, “between pecuniary and industrial employment”, “between those who make money and those who produce socially useful goods and services, etc”²⁹. Finally Viano (2005, p.241) recently wrote “[Veblen] believed that struggle is a constant trait of modern societies and shapes all aspects of their institutions”.

Next to the idea of conflict over the distribution of resources – which will be reconsidered in chapter 3 –the literature has given less emphasis to micro conflict, that is to say to conflict within firms between undertakers and technicians, which can be recognized as the main cause of unemployment in Veblen. So unemployment appears to be determined by the outcome of the conflict within the firm, involving contrasting aims and contrasting instincts, and in particular its level depends on the result of conflict between undertakers and technicians. Let us see why: the conflict between undertakers and technicians is not a conflict over the necessities of life. It is a conflict between *tendentially* incompatible instincts. undertakers in fact pursue the aim of monetary profits *via* predatory instincts while technicians are interested in expanding production *via* the use of new scientific knowledge being driven by the instinct of workmanship. So conflict between undertakers and technicians derives from the ‘clash’ between *tendentially* incompatible instincts: workmanship against predation.

²⁹ So unlike neoclassic economics Veblen looks at the economy in *non-cooperative* terms. As remarked by Realforzo (1995, p.18) the market economy is assumed to be cooperative for two main reasons: *a*) “absence of powers and class struggle”, *b*) working of “a principle of distributive equity” (see Clark, 1965 [1889]). In particular the two points are closely connected since each agent is assumed to be completely free to take her/his decision on *how*, *where* and *what* to produce. In addition if each agent is free to choose how to participate in production s/he will obtain remuneration that will be exactly proportional to her/his contribution. In addition, if the remuneration is proportionate to the contribution to production, then remuneration is in fact considered fair. Consequently, conflict does not occur since each agent knows perfectly what contribution to the production has been given and what remuneration is due. However conflict is not completely excluded and it is connected to market rigidity. In fact when the market economy works correctly, all markets are in equilibrium since flexibility of prices allows the equality between demand and supply. As a result, conflict does not occur if flexibility of prices is guaranteed since in this case each agent is able to reach an equilibrium between what s/he asks for and what s/he supplies. If conflict exists markets are not actually in equilibrium and in fact this is possible if an external rigidity does not allow the equality between demand and supply (cf. Forges Davanzati, 1999, p.11). In addition in a market economy the equilibrium of the markets ensures that the conflict is in fact removed *ex ante* since each agent has collected all the information that is needed to obtain an effective result equal to the expected one. This point is well expressed by Basile and Casavola (1992, p.10) who remark: “[...] in the Walrasian world agents must agree *ex ante* on all the relevant variables [...] As the information structure is complete, time is irrelevant and terms of trade are always known to the agents *ex ante*. Conflicts of interest and related problems of enforcing terms of transactions do not come to the surface as they can be solved by a costless long-term contract”.

The result of this conflict is the definition of a level of production in line with the decisions of the ‘winners’ of the conflict, and the effects of these decisions have a positive or negative effect on the level of employment. If predation defeats workmanship then production and employment decrease; on the other hand, if workmanship defeats predation then production and employment increase. More specifically, both undertakers and technicians mainly define their own production target according to the intensity of their own instinct. The predation of undertakers is shown in the desire to obtain the maximum competitive advantage in terms of profit while the workmanship of technicians is shown in the desire to obtain the maximum production for giving concrete form to their efficiency, knowledge and skills. It is possible that the production function of the firm – that could be called *workmanship function* – is composed of the following variables – (see O’Hara 2000, p.72) – *a*) technology, *b*) workers’ skills and knowledge and *c*) the “stock and rate of utilization of the available capital stock”. Given this representation of Veblen’s hypothetical production function, it is possible to assume that the technological state, the state of knowledge and skills and the stock of capital are given in the short run; as a consequence, the effective production depends only on the degree of utilization of capital. The number of workers employed in the firm becomes a function of the capital stock and rate of utilization, and since the capital stock is given, the number of workers becomes a function of the rate of capital utilization³⁰. Given the technology, knowledge, skills and stock of capital, the production can be definable as a function of the demand for labour which in turn becomes a function of the rate of utilization of capital. If the rate of capital utilization increases then employment increases too and *vice versa*. If employment is a function of the rate of utilization of capital then we need to investigate this rate. We can consider the degree of capital utilization to be equal to the effective output/potential output ratio. Potential output is an increasing function of the technicians’ production aim given information on the non-bankruptcy condition. Effective output is instead the result of the conflict between undertakers and

³⁰ Implicitly here the production function is assumed at constant return in line with a non marginalist construction of models and in absence of alternative and clear positions by Veblen. Mouhammed (2003) argues that – with the theory of economic growth (see § 2.3) - Veblen removes validity from the law of decreasing return of inputs. On this point Mouhammed (2003, p.151) writes: "Technology (the industrial arts or the joint stock of knowledge) is a social ownership of the community and is accumulated over time. However, by private ownership of the means of production capitalists invariably manage to appropriate the benefits of the technological advantages, which should have been imputed to the community. Thus, for Veblen, the neoclassical marginal productivity theory cannot be applied either to the tangible (or the durable part of the capital) or to the intangible part".

technicians given the expectations on demand on the part of undertakers. So it is possible to define k^* as the undertakers' goal of capital utilization and k^0 the technicians' goal of capital utilization. The effective rate of utilization of capital is the result of conflict between undertakers and technicians. In fact conflict occurs when k^* is different from k^0 and the intensity of conflict depends on the bargaining power of undertakers and technicians, which depends on: *a*) the technicians' degree of docility, which in turns depends on the wage they are paid; it is reasonable to think that the higher the wage, the higher the docility of technicians in the conflict against undertakers, *b*) the extent to which the firm is capital intensive since it can reasonably be argued that the higher the capital/labour ratio, the more necessary technicians are in implementing the production process and *c*) the number of technicians. Points *b* and *c* are strictly connected since in both cases the bargaining power of technicians is high; in fact when the capital/labour rate is in favour of capital, technicians are more necessary for undertakers. Consequently while the number of workers is reduced the number of technicians is increased, and as a result technicians acquire a higher bargaining power than undertakers³¹.

³¹ Note that considering the position played within the firm it is reasonable to think that technicians have more bargaining power than workers so they have higher wages. The wage differential existing between technicians and workers is not simply the result of the differential of skills and efficiency between them but it is probably the result of the conflict that naturally exists within the firm between undertakers and technicians. In other words the wage differential can be seen as a "discipline device" for technicians or rather as a tool for assuring their docility and avoiding conflict. As Veblen writes "by settled habit the technicians, the engineers and industrial experts, are a *harmless* and *docile* sort, well fed on the whole, and somewhat placidly content with the "*full dinner-pail*" which the lieutenants of the Vested Interests habitually allow them" (Veblen, 2001 [1921], p.83; italics added). Moreover, one could argue that the undertakers' bargaining power increases if the technicians' unemployment rate increases since undertakers could obtain the docility of technicians with a strong threat of dismissal. Supposing there is high undertaker bargaining power, the docility of technicians increases; as a consequence the undertakers' predatory instinct 'swamps' the technicians' instinct of workmanship, and the more docile the technicians, the easier it is to control and under-use capital. This in turns determines a reduction of real production, a reduction of employment, an increase in prices and an increase in monetary profits. Expanding the Veblenian theory of under-utilization of capital it could be argued that the bargaining power of firms increases if policies of deregulation of labour market are in place. Deregulation of the labour market includes two kinds of arguments: *a*) deregulation of the labour market in the strict sense (sometimes simply called deregulation of the labour market) and *b*) deregulation of the labour contract. The first type of deregulation places limits on the presence of the State – and other institutional organizations (Trade Unions above all) – during the bargaining between firms and employees over wages and unemployment benefits. On the other hand, deregulation of the labour contract eliminates constraints on the influence of the State – and other institutional organizations – over working hours, firms' freedom to hire and fire and workers' mobility within firms. Here with the term 'deregulation of the labour contract' will entail considering both the deregulation of the labour market in a strict sense and the deregulation of the labour contract. So policies of labour market deregulation could have a negative effect on the level of production, and as a consequence, while the degree of capital utilization falls, unemployment, prices and profits rise. In brief, the Veblenian theory of under utilization of capital could also explain a probable process of stagflation. More specifically, if there is unemployment and policies of deregulation of the labour market, then the threat of dismissal of technicians becomes more

The rate of utilization of capital taken as the technicians' goal is however subject to constraints and it is reasonable to think that k^0 meets a constraint in the *non-bankruptcy* condition, i.e. the firm does not produce at a loss but at least at a nil profit. On the other hand k^* is determined on the basis of market demand which has an upward or downward slope and is tendentially inelastic. Veblen implicitly assumes that all goods produced are goods with a low degree of replaceability and Sweezy (1957) and Arrow (1975) argues that the market structure is one of monopolistic competition. There is another important consideration to make: Veblen does not rule out an upward sloping demand curve, so that demand increases if the price of goods increases (particularly for luxury goods), an effect that in the literature has been called "the Veblen effect" (see Leibenstein 1950; see also ch.2). It is important to notice – although Veblen does not directly remark on this point – that his theory of under-utilization of capital can be built on the implicit assumption that this effect is not in operation; in fact if this effect were in operation the internal conflict would not occur since the aim of maximization of production for technicians would also be the aim of the undertakers. So the undertakers' opposition to the maximization of production is connected to the nature of the goods produced or to the policies of differentiation put in place by undertakers *via* business activities when the Veblen effect is absent.

realistic, and their market wage can be reduced as well. The undertakers' bargaining power increases and that of technicians declines; as a result, the conflict between undertakers and technicians is to the advantage of undertakers, who reduce production – determining a reduction of employment – while prices and monetary profits increase: Deregulation has therefore generated stagflation (see also Pacella, 2005a, 2005b; 2006a). In addition if the threat of dismissal increases and if wages decrease (in the whole working class) the demand for wage goods diminishes. In this case the degree of capital utilization decreases again and its under-utilization is no longer profitable since demand is low. In this case, the system works by an additional reduction of the degree of capital utilization, which makes unemployment rise and prices and profits fall. In this case a vicious circle could be generated if policies of regulation are not introduced. In fact if profits decrease, undertakers could react with an additional wage cut, but this would push them to make an additional reduction of demand, which would a drop in production, employment, prices, and profits. Since an endogenous change appears to be unlikely due to the predatory nature of undertakers, then policies of labour market regulation become essential. These in fact bring about an increase in employment and production via the increase in wages and/or the reduction of threat of dismissal thanks to the increased bargaining power of technicians, who can now give concrete form to their instinct of workmanship through the increase in production, and thanks to the increased demand to which undertakers react by raising production at least up to a profitable level.

Chapter II

PRODUCTION, INCOME DISTRIBUTION AND ECONOMIC GROWTH

2.1 Credit, prices and the circuit of income

As anticipated in chapter 1, alongside the idea of conflictual economy, the Veblenian macroeconomic process is built with the additional hypothesis that the *current* economy is a credit economy. In the *Theory of Business Enterprise* (ch.6) Veblen makes a brief evolutionary analysis of the role of money in the economy. Here he stresses that the economy was primarily a “natural economy”, which then changed into a monetary economy and finally into a credit economy: the *current* economy. Veblen distinguishes the three economies on the basis of the goods exchanged and the aim of these exchanges. More specifically, Veblen remarks that in the “natural economy” the main market is the commodities market in which the goods exchanged are the outputs which are exchanged with the aim of having sources of material serviceability; in the monetary economy the main market continues to be the commodities market but outputs are not exchanged to obtain goods but to have just one good: money. However – Veblen adds – the possibility of making money depends on the capacity to produce goods that provide a material serviceability. On the other hand the credit economy – Veblen stresses – is an economy in which the institution of ownership and the “pecuniary principles” are the “spiritual fonts” of firms (see Veblen, 1904, ch.4). In such an economy, credit has a fundamental role in production. More specifically in Veblen’s vision “credit is an expedient of business [and] business men resort to credit for the sake of gain being counted in money values” (Veblen, 1905, p.461). In particular Veblen gives credit two functions: *a*) the function of “loans or debts – notes, stock shares, interestbearing securities, deposits, call loans, etc”. (Veblen, 1904, p.92) and *b*) the function to postpone payments (see Veblen, 1904, ch.5)³². While the first

³² With reference to the second function of credit Veblen states that the industrial system is a complex structure based on a construction of interdependent relationships formalized by contracts of purchase and sale amongst firms. Such contracts define sales and purchases in terms of monetary values and are regularized by credit agreements under the specific form of postponement of payments (see Veblen, 1904, ch.7).

kind of credit precedes production the second one follows it. Consequently it is reasonable to think that Veblen makes reference to “loans or debts” as tools for financing production³³. The issue of credit as loans or debt is widely studied by Veblen, in particular under two main aspects: *a)* its relation with the formation of prices and *b)* its relation with the formation of profits. While the topic of credit-profits will be examined in section 2.2.2 here let us see the credit-prices relation. In particular according to the author, in a monetary economy the variation of prices depends: *a)* on the variation of quantity of money demand of firms, that is to say the demand for credit; *b)* on the variation of interest rate. Let us see the first point. Veblen has a clear idea that an increased money demand by firms is a sufficient cause of the increase of prices. His work “*Credit and Prices*” (1905) is the main source with which it is possible to explain why a causal relation exists between money demand by firms and prices. As Veblen writes:

“A pronounced advance in prices [that] results in an increase extension of credit seems plain from what happens during a [...] speculative advance (Veblen, 1905, p.461) [and] closely related to the expansion of credit [...] is a large volume of new capitalization” (Veblen, 1905, p.463).

In Veblen money is demanded to obtain profits and – according to the author (see § 2.2.2) – profits increase if the firm’s dimension increases. Why this happens will be explained in section 2.2.2. Here it is sufficient to say that Veblen always assumes that the firm’s size is the competitive factor, that is to say the factor that assures profitability to firm. More specifically Veblen stresses that firm size is functional to the realization of monopolist markets, in which undertakers can obtain high profits *via* the control of prices. The consequence is that the higher the money demand, the greater the firm’s size and the higher the prices.

³³ Using money as a financing tool is different from its use as a payment tool. In the last case money serves to obtain the ownership of the use of given products and services. In other words the use of money as a tool of payment releases the purchaser from the obligation to pay as soon as the product or service is bought or used. This also means that the product or service has been produced, is being produced, or will be produced independently of the existence of money. In brief, money supplies serviceability just in the moment of exchange, and therefore in a subsequent phase of production. On the other hand if money is used as a financing tool then it supplies serviceability in the starting phase of production. In other words the existence of products and services presupposes the foregoing existence of money and not *vice versa* (see Graziani, 2003; Realfonzo, 2003). Following Graziani’s distinctions (2003) between pure monetary economy and pure credit economy, one can classify Veblen’s picture as a monetary-credit economy or simply – as Veblen sums it up – as a credit economy since he often speaks at the same time about money as a financing tool and a tool of payment. Veblen’s theory of the monetary-financial market is also interesting because the author puts the financial market on the same level as the monetary market in the phase of financing production.

Veblen however remarks that the use of credit is not only motivated by monopolist aims. In fact competition itself is a cause of the increase of money demand and increase of prices. More specifically, due to competitive pressure the individual firm is forced to expand its capital via the use of credit, but “since the advantage to be derived from this expedient is a competitive advantage only, the universality of the practice results in but a slight, if any, increase of the aggregate earnings of the business community” (Veblen, 1904, p.98). Insofar as firms are not homogeneous, the credit system tends spontaneously to contribute to the increase in the size of the biggest firms: “since an advance of credit rests on the collateral as expressed in terms of value” (Veblen, 1904, p.105), firms with a higher amount of collateral obtain a higher amount of credit and, hence, can expand, thus gaining further advantages over their (smaller) competitors. As a result, an ‘imperfect’ credit market is likely to spontaneously generate a selection of firms on the basis of their collateral, thus allowing the expansion of the bigger firms and the possible bankruptcy of the smaller firms. Moreover, the bigger firms can increase their prices thanks to their additional enlargement but also because the increase of bankruptcies reduces the aggregate output. Note that, in both cases, bank-firm relationships do not affect the volume of aggregate production, but simply redistribute aggregate profits among firms³⁴.

Let us see the second point. As we have seen above, Veblen structures a positive relation between quantity of money demand and profits (see § 2.2.2). On the quantity of money demanded firms have to pay interest. Interest is seen by Veblen as financial cost that can reduce profits. In other words Veblen himself defines an inverse relation between interest rate and profit rate since – given a firm’s size – the increase in interest reduces profits since financing costs increase and revenues are the same. As Veblen argues, a variation of the interest rate, in fact, “diminishes the *aggregate* net profits [...] in that it requires them to pay interest” (Veblen, 1904, p.112; italics added).

³⁴ On the interpretation of the determination of prices and possible inflationary consequences in Veblen’s thought, Mouhammed (2003, p.163) stresses that in Veblen’s thought: “i) prices [...] are created by large corporations through restricting the output of the machine industry in order to generate required rates of profits; ii) they can depend on the increased money supply; iii) they can be generated via social conflict within the firm, since “unionised workers can slow down productivity and thus increase the per unit costs of output, a condition that forces producers to raise relative prices in order to defend their rate of profits” (On the effect conflict-inflation see also § 3.3c).

The decrease of profits can push firms to disinvest and as a result, output decreases and prices increase. At the same time however the process of disinvestment does not appear so obvious; in fact if financing costs increase firms can reply by merging operations that lead to an increase in size and therefore in prices. In other words new capitalizations are not necessarily stopped if interest rates increase since “[the] large volume of new capitalization [can also have] the form of new incorporations or expansions and coalitions of corporations already in existence” (Veblen, 1905, p.463).

Since: *i*) the functioning of the credit market contributes to expanding firm size and *ii*) a positive relation between firm’s capitalization and its profits is assumed, one can draw the following conclusion. In Veblen’s view, high profits derive from high prices (and low levels of production), and high profits derive from high volume of finance: as a result, *the higher the amount of finance, the higher the price level*. Moreover, since the increase in the interest rate reduces *aggregate* money profits, one can argue that two possible reactions on the part of firms are in order: *a*) they increase prices, if demand is high enough (i.e. the argument of “what the traffic will bear”) and this strategy is likely to be effective in the event that the functioning of the credit market determines a lower intensity of competition in the market for goods; *b*) in the opposite case, the increase in the interest rate generates disinvestments (hence, a drop of output and the consequent price increases). In both cases a direct relationship between interest rate and the price level holds.

Given the above premise on the Veblenian credit economy let us show a possible representation of the Veblenian circuit of income in the following figure:

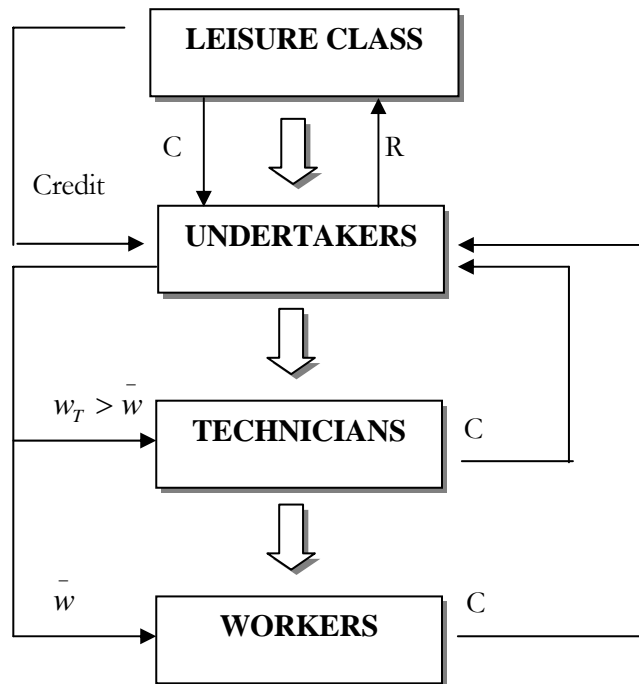


Figure 1: The Veblenian circuit of income I³⁵

The Veblenian circuit of income is formed by the working of two main markets: *a*) the monetary-financial market (generally understood as the credit system) and *b*) the commodities market with the first preceding the second. In addition in the Veblenian circuit of income three classes are involved: *a*) the leisure class, that is to say the financiers' class; *b*) the undertakers, that is to say the class of manager-owners of firms and *c*) the class of technicians and workers. From the above schema it can be said that the leisure class directly controls undertakers and indirectly technicians and workers³⁶. On the other hand, undertakers directly control technicians and indirectly workers. Finally technicians directly control workers³⁷. The leisure class is

³⁵ C = consumption, R = reimbursement of loans.

³⁶ It is important to notice that Veblen is not steady in maintaining a clear opposition between the leisure class and undertakers. Consequently the possibility that undertakers are also members of leisure class is not completely excluded by Veblen in his writings even though for the purpose of the present work the hypothesis of the overlapping between leisure class and undertakers is not taken into consideration.

³⁷ Before showing Veblen's circuit in detail it would seem useful to give a brief description of Marx's money capital circuit (*Capital* Vol 2 part 1; see on this point the clear description presented by Bellofiore, Forges Davanzati and Realfonzo, 2000). This description is useful for a better understanding of Veblen's circuit since Veblen seems to want to maintain the Marxian logic chain of money-goods-money even if in describing the monetary economy Veblen does not explain the determinant of profits as in Marx; he in fact limits his hypothetical analysis of the circuit of income to the role of money in the sense that for Veblen the process starts from money and finishes in money *via* the commodities market without however tracing the origin of profits within the production process. In addition note that a

superordinate to the other social classes; its superordinacy is due to its capacity to control the monetary-financial market; the control can be direct when the leisure class manages the banking system or indirect when the volume of money is mainly concentrated in its hands. More specifically the leisure class controls the credit sector mainly on the side of quantity of financing supplied, since it owns the right to the production of money historically acquired; it also sets the interest rate at which they are interested to supply the financing. Moreover members of the leisure class can control firms also by means of the ownership of firm's stocks (often called intangible assets):

“The free income which is capitalized in the intangible assets of the vested interests goes to support the well-to-do investors, who are for this reason called the kept classes, and whose keep consists in an indefinitely extensible consumption of superfluities” (Veblen, 1964 [1919a], ch.5).

considerable part of the literature sees Veblen as proposing the Marxian vision of capitalism. On this point see for example Harris (1958), Knight (1969), Sowell (1987). Rutherford (1984, pp.121-122) for example argues that “there is [in Veblen] a dialectic reminiscent of Marx: the internal logic of a system giving rise to contradictions that create its own transformation”. In addition O’Hara (2000, pp.67 ff.) remarks that “strong associations between Marx and Veblen” exist; in particular the author remarks that both the authors in fact accept the idea of the materialistic conception of history and they both place importance on the “technological and social relationship” of capitalism even if the approach to the “directive motion” of capitalism is in fact absent in Veblen. Like Marx – O’Hara adds – Veblen finds positive aspects and negative aspects of capitalism; in Veblen for example the main positive aspect is the development of technology, while negative aspects are “long-term crises, the private expropriation of the economic surplus by the vested interest, the financial domination of industry, etc.”. On the other hand, Edgell and Townshend (1993, p.313) point out that Veblen’s thought appears to be different from Marx stressing that “Veblen’s theory of increasing status competition, expressed in terms of a ‘struggle to keep up appearances’ is alternative to Marx’s theory of increasing class conflict”. Now let us briefly describe the Marxian’s circuit. As we know, Marx’s circuit of money capital features three steps: *a*) the use of money for the purchase of inputs (raw materials and labour force); *b*) the process of production and valorisation – in quantitative terms - of outputs; *c*) the selling of outputs at a higher value than that of the inputs employed. The surplus obtained by the sale is ploughed back into the purchase of new inputs to start a new circuit: *accumulation for accumulation*. As also remarked by O’Hara (2000, ch.2), Marx considers the buying and selling phases as movements of “formal capital” which in fact is the expression of the separation between social classes: the capitalists that own the means of production and who need workers for the production of a surplus and workers that just own their own labour force and need capitalists so as to obtain wages. The commodities market and labour market are the main markets on which Marx bases his theory of circuit of capital where the labour market is superordinate to the commodity market (cf. Veblen’s credit economy). Capitalists meet workers at the labour market; here capitalists sell their own money capital in exchange for labour force, then they use the labour force to produce outputs with a higher value than what was advanced for them; such outputs are then sold into the commodities market and here capitalists obtain the money capital advanced to workers plus the surplus originating in the production phase. The process of valorisation of outcome is not identified by Marx in the lattermost phases (purchasing and sale) but in the movement of “real capital” in other words in the production process. Marx sees the labour force as source of surplus since the means of production cannot add more value to the outcome than what was absorbed by them. In Marx, value is the quantity of labour employed in the production, so if a mechanical tool has been produced by – for example – 40 hours of labour then its contribution to the valorisation of new products cannot go over 40 hours. On the contrary this limit does not occur for workers and the size of the surplus is equal to the difference between the labour that is needed to produce outputs and the labour that is necessary for the production that assures the workers’ subsistence.

Note the kind of control of the monetary market is not equal to the kind of control of the financial market. In the monetary market the leisure class can control the price of financing – that is to say the interest rate – while the quantity of money depends on firms’ demand. At the same time in the financial market the leisure class can control the quantity of financing by the acquisition of stocks and bonds issued by undertakers but not their remuneration since while the remuneration of stocks depends on dividends produced by firms the remuneration of bonds depends on the interest rate fixed by undertakers, even if it is reasonable to think that undertakers fix the interest rate with reference to the interest rate of the monetary market.

In view of what has been said, although Veblen includes a variety of subjects within the leisure class for the purpose of the interpretation proposed here the leisure class is assumed to be formed *only* by those who obtain money gains without directly contributing to the production of goods: namely, financiers, rentiers and bankers. Although Veblen does not stress this point it would be possible to attribute the role of “captain of finance” to the leisure class; the term is used here to indicate the pre-eminent role at the top of the industrial system, serving to finance the production sector, and in opposition to the role of “captain of industry” given to undertakers³⁸.

³⁸ In fact Veblen is not clear in distinguishing captain of industry from captain of finance; he sometimes uses the terms synonymously; other times he seems to give the name captain of industry to financiers and sometimes he gives the name captain of finance to undertakers; so the owners are sometimes financiers and undertakers are simple business men, therefore mere managers (see Veblen 2001 [1921], ch. II and III). This lack of clarity is due to the fact that the idea of financier in Veblen is broader than may be imagined. In other words the distinction between captain of finance and captain of industry would be clear if the financier granted his/her financing only by forms of credit agreement; in this case the separation of the figure of creditor and owner of the firm is clear. On the other hand when a financier grants financing through operations of copartnership in the capital of firm than the figure of financier mingles with the figure of owner and in fact the captain of finance is also captain of industry. In the present work however greater emphasis will be placed on separating the roles of captain of finance from captain of industry for the purpose of investigate how the economic choices of the top class of the industrial system can affect the working of the economic system as a whole. At the same time Veblen sometimes calls undertakers captains of industry or businessmen and on this point Veblen writes “captain of industry [is] the absentee owner and controller of industrial equipment and resources” (Veblen, 1967 [1923], p.70). According to Dixon (2002, p.202) Veblen’s theory of “captain of industry [...] posed serious issues for economic analysis and political economy [such as]: What were the implications of the rise of this class of people [...] for theories of income distribution? What were the implications for likely future relations between labor and capital?”. In view of what has been said above, undertakers and financiers can be a single unit or separate units. One could argue that Veblen separates undertakers from financiers not on the level of their aim – both undertakers and financiers act to obtain pecuniary gains – but in the sense of expertise. On this point Veblen for example remarks that “it is currently believed, probably on sufficient grounds, that the corporations can make more profitable use of the property than the buyers of the securities, particularly a more profitable use than the buyers could make of it without spending additional time and attention in the management of the property” (Veblen, 1905, p.463). However Chypher (1988) interpreting Veblen does not distinguish financiers from undertakers remarking on the possibility of a direct management of industry by the financial sector. On this point Chypher (1988, p.78) states that “the Veblenian dichotomy between “Captain of industry” and

The leisure class is the main “pecuniary class” in the society; in addition if Veblen defines the leisure class as the pecuniary class then it is reasonable to think that the primary good sought by the leisure class is money and money is accumulated and used by the leisure class for purposes of ostentation; in the same time members of the leisure class are excluded from productive activities; this necessarily calls for different activities from which the leisure class can obtain money. The simplest way of accumulating money without engaging in productive labour is the accumulation of money from money and the activity of financing – by the monetary and financial market – appears to be the first way in which the leisure class, in line with its own traits, obtains money. As Veblen remarks:

“The relation of the leisure class [...] to the economic process is a pecuniary relation – a relation of acquisition, not of production; of exploitation, not of serviceability” (Veblen, 1975 [1899a], p.209).

He also adds: “indirectly their *economic office* may, of course, be of the *utmost* importance to the economic life process” (Veblen, 1975 [1899a], p.209; italics added) and in a context of a *current* credit economy the most important “economic office” is the monetary-financing sector. There is another interesting quotation that can be considered for the purpose of extending the role of the leisure class to the banking sector. Veblen stresses that:

“The changed industrial life requires changed methods of acquisition; and the pecuniary classes have some interest in so adapting the pecuniary institutions as to give them the best effect for acquisition of private gain that is compatible with the continuance of the industrial process out of which this gain arises” (Veblen, 1975 [1899a], p.209).

On the above quotation it is possible to remark that the process of exploitation of the leisure class derives from the adaptation of “pecuniary institutions” to the “industrial process”; without such adaptation exploitation is not ‘justifiable’. In other words, if money did not have an institutional role as a habit of the production and distribution of income then the social role of leisure class would be nil. In consequence the money-goods-money relation in Veblen seems to have a strong institutional base. It is a

“Captains of Finance” no longer existed [since] investment bankers who dominated the financial sphere intermingled with those who operated the [...] industries”.

“habit” and – expanding Veblen’s thought – a habit of thought instrumental to the current perseverance of the leisure class.

Hence – interpreting and expanding Veblen’s idea – the control of the monetary-financial sector is the task of the leisure class for two main reasons: *a)* the leisure class owns money and *b)* the financing activity is a concrete example of unproductive labour typical of members of the leisure class. The execution of a pure credit activity suits the leisure class since it is both a deserving activity and a font of income; moreover, it supplies a font of income without the need to make any kind of effort. In particular, monetary-financial activity is a non-productive activity in a strict sense; at the same time it is “decent” since it is ‘serviceable’ to the collectivity in the sense that it serves for financing production; in addition it is “conventional evidence of wealth” since the leisure class has money which conventionally represents the fundamental resource for the economy and sign of social status. In brief the conventional right to the abstention from labour is a consequence of the possession of money, which is a conventional trait of conspicuous leisure.

The above leisure class and undertakers are allocated in the circuit. More specifically undertakers meet financiers in the monetary-financial market selling promises of payment (by bonds, loans, etc.) and company shares in exchange for the financiers’ money: “pecuniary capital”. The aim of undertakers and financiers is to increase the value of money capital bought and sold in the monetary-financial market, in other words undertakers want to have profits, financiers want to have monetary gains (interest, dividends)³⁹. The demand for monetary capital is in the hands of undertakers and depends on expected profits and on the cost of financing; moreover the expectation of profit depends on the expected demand and also on conjectures on the behaviour of its competitors. In the monetary-financial market undertakers establish the monetary capital of their own firm, then they invest this capital acquiring tools for generating income. This point will be investigated in greater depth in the section 2.2.2 but here it is useful to notice that Veblen divides capital into “intangible” – think for instance of brand-names - and “tangible” goods or assets (mechanical equipment); at the same time undertakers employ a number of workers proportionate to the necessities imposed by the management of mechanical equipment and to the execution

³⁹ Dividends being portions of profit, financiers also formally become undertakers; however if their contribution to the management of the firm is purely nominal then in practice they continue to play the role of financier of the firm.

of business activities. The capital owned by undertakers is then used for producing goods and services which are then sold on the commodities market. Here the pecuniary capital is recovered.

The role of workers is simply instrumental for undertakers since the concrete management of machines and the execution of business activities is attributed to technicians, while the choice of entity of capital and its strategic differentiation between tangible and intangible asset is at the basis of the making of profits. In view of what has been said, three main variables affect the quantity of financing: the supply of financiers⁴⁰, the price of financing and the expected profits of undertakers. The initial process of production depends on the undertakers' decisions on the type and size of tangible and intangible capital chosen for the firm's activity. The number of workers and technicians employed will just depend on the necessities connected to the management of tangible and intangible capital. In Veblen therefore the labour market is a 'residual' market in the sense that the level of employment is not set via the intersection between the demand for labour and labour supply; moreover, wages are different for workers and technicians, in fact, two wage levels are identifiable: *a*) a money wage for the payment of workers which is negotiated by undertakers and workers \bar{w} and *b*) a wage for technicians w_T which is negotiated by undertakers and technicians and is higher than the subsistence wage. Technicians and workers are subordinated to undertakers since they are dependent workers while workers are subordinated to technicians since they depend on the instructions of their technical managers. Note that wage is paid by the monetary capital of undertakers and/or by monetary capital of leisure class. When workers and technicians receive their wage – which is paid in advance – they start production of goods and services⁴¹; when production is completed the output is allocated in the market at a profitable price fixed by the firm. All the classes contribute to the consumption of output whose quantity is however maintained at a level lower than the real needs. The limitation of production maintains prices at a high level and also helps to recover the pecuniary capital in a brief time. The pecuniary capital recovered on the commodities market will be paid back to financiers (owners of bonds and credit agreements) or eventually maintained

⁴⁰ Although Veblen also recognizes the possibility that the financing of production is guaranteed by the firm itself by the process of self-financing, re-investing the profits realized (see Veblen 1904, ch.5 and ch.6).

⁴¹ Supposing that firms are vertically integrated.

within the firm (if financiers are joint owners of the firm). In both cases the pecuniary capital recovered will be used afresh for new capitalization and production.

Different authors look at Veblen's circuit of income production in terms of monetary-credit economy. Dillard (1987) for example argues that in Veblen's vision the money supply is in fact endogenous, the interest rate is a pure monetary phenomenon and production starts with the demand for 'initial finance' on the part of firms. Moreover the author finds significant analogies between Veblen's and Keynes's views of the functioning of monetary economies. On this point Dillard (1987, p.1646) writes: "Money is a form of private property that wealth holders in business enterprise economy at times treasure more than income itself. It is a device for limiting losses in a profit-and-loss economy. The moral of Veblen's teaching is that in a pecuniary economy, monetary values dominate industrial values" (Dillard, 1987, p.1646)⁴². Moreover Parker Foster and Ranson (1987, p.228) maintain that "The conclusion reached by both Veblen and Keynes is that the traditional theory of production is flawed. Production is governed not by real exchanges but by the institution of money. Production continues only as permitted by the creation of new credit to finance new investment". In line with Dillard and Parker Foster and Ranson, Mouhammed (2003, p.279) concludes that Veblen developed a model of the monetary theory of production, where although "a lucid explanation for the interest rate determination" is not provided, the pricing markup can be used to determine it within the Veblenian theoretical framework⁴³. Rutherford (1980, p.439) expands this argument by arguing that: "No firm can survive in the 'credit economy' of the New Order that fails to fully extend its credit; and so become dependent on the banker"⁴⁴.

The above schema however can be developed; Veblen in fact divides the commodities market into two sectors: *a*) one sector producing luxury goods and *b*) another producing wage goods. These parallel commodities markets are not integrated – differently from the sector of capital goods – in the same firm because of different

⁴² In comparing Veblen's and Keynes's thought, Mouhammed (2003, p.268) stresses that "Veblen believes (as Keynes does) that the interest rate and the money supply are used to control the economy by the vested interests". He also attributes to Veblen the Keynesian principle of effective demand, arguing that a 'vent for surplus' argument via imperialism is relevant in Veblen's thought (pp.273 ff.).

⁴³ See Graziani (2003) for a general description of the monetary theory of production.

⁴⁴ Phillips (2002) builds a Veblenian model of financial instability where the dynamics of credit market significantly affects the path of production. In particular, the author shows that "a rise in price of capital will have two effects: one will be to lower the demand for capital and the other will be to induce banks to increase loans since from their point of view there is an apparent increase in net wealth". As a result, due to the functioning of the credit market, economies are intrinsically unstable.

technical and business competences required by the two sectors and because of the peculiarity of demand expressed by the leisure class and workers (see §§ 2.2.1.1 and 2.2.3)⁴⁵.

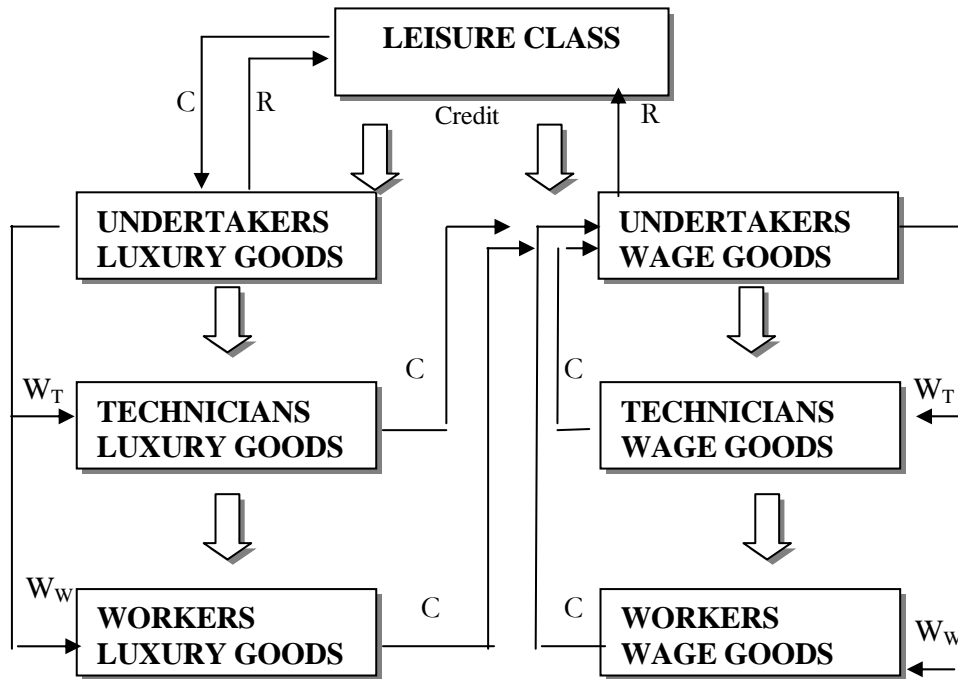


Figure 2: The Veblenian circuit of income II

The main difference between *Figure 1* and *Figure 2* mainly concerns the circuit of consumption. In particular this figure shows that the level of financing and its price are defined on the basis of type and quantity of consumption. In particular while the leisure class mainly consumes luxury goods – since it is interested in conspicuous and competitive consumption (see § 2.2.1.1) – technicians and workers just consume wage goods. In addition, no consumption is made by undertakers; these are mainly interested in accumulating monetary profits⁴⁶. An observation can be made here: while the leisure class is interested in accumulation for consumption, undertakers are interested in accumulation for the sake of accumulation. So Veblen's capitalist system is a system that acts for the reproduction and enlargement of the capital of the leisure

⁴⁵ W_T = wage of technicians and W_W = wage of workers.

⁴⁶ In fact Veblen is not clear on the utilization of profits; he clearly stresses that undertakers work to obtain profits but he does not discuss their subsequent utilization. There are two possibilities: *a*) undertakers re-invest profits and *b*) undertakers consume profits both in the market of luxury and wage goods. Since the aim of undertakers is to obtain profit then in the present work the main hypothesis remains that undertakers continually re-invest their profits.

class and for the reproduction and enlargement of undertakers' capital where consumption is the determinant of accumulation for the leisure class while profit is the determinant of accumulation for undertakers⁴⁷. Another observation is useful here: even if Veblen does not directly define the luxury good, this can be seen as an expression of symbol and trophy in a logic of conspicuous consumption. Even though the question will be more clearly examined in the section 2.2.1.1 here it is important to give some anticipations. Luxury goods are prevalently goods conveying information about the purchaser's social status, standard of living and lifestyle and success in society⁴⁸. So the motive of the consumption of luxury goods is neither "the consumer's physical wants" nor the "higher wants – spiritual, æsthetic [or] intellectual"; it is simply a tool for the demonstration of conspicuous social position, whether this is provisional or not (see Veblen, 1975 [1899a], pp.25-26). Veblen tries to give such features to these goods. In particular in his vision, luxury goods must be at the same time: *beautiful, qualitatively superior to others, futile, with low reproducibility and costly* (see Veblen, 1975 [1899a], p.176). On these points, for example, "hand labour is a more wasteful method of production" writes Veblen (1975 [1899a], p.159). Then he adds: "let us remember that our higher appreciation of the superior article is an appreciation of its superior honorific character" (Veblen 1975 [1899a], p.128). Actually the character of non-reproducibility – or limited reproducibility – is a necessary condition for assigning a high value to things but it is not sufficient since the high value is mainly recognized in the capacity of the thing to supply high gratification which can be of different kinds such as gratification for its "futility" (Veblen, 1975 [1899a], p.137) and gratification of our "sense of costliness masquerading under the name of beauty" (Veblen, 1975 [1899a], p.128). In addition since "the utility of articles [...] depends closely upon the expensiveness of the articles" (Veblen, 1975

⁴⁷ In the Veblenian schema the aim of production is twofold: consumption and accumulation and it is different from the Marxian schema of capitalistic production and from the Marxian schema of *pre-capitalistic* production. Unlike the Marxian capitalistic schema of production – in which the aim of production is the increase of exchange values – in the Marxian *pre-capitalistic* schema the aim of production is the increase of use values. More in detail, in the Marxian *pre-capitalistic* schema production only serves for the satisfaction of needs. In the commodities market the productive unities meet in order to sell the goods produced in exchange for money, which allows the purchase of other and different goods which in turn increase the level of satisfaction (and therefore the use values. In brief, use value is the reason for exchanges in the *pre-capitalistic* phase and the circuit becomes goods-money-goods.

⁴⁸ The standard of living can be defined in different ways; amongst others, Waite and Cassidy (1949, pp.216-217) define the standard of living "the goods, services, and conditions which an individual or group earnestly strives to attain, to maintain if once attained, and to regain if lost".

[1899a], p.126), the higher the admiration of one or more particularities of a thing, the more willing one is to pay a high price for that thing. As Veblen writes:

“The mark of expensiveness come to be accepted as beautiful features of expensive articles (Veblen, 1975 [1899a], p.130) [...] The consumption of expensive goods is meritorious, and the goods which contain an appreciable element of cost in excess of what goes to give them serviceability for their ostensible mechanical purpose are honorific” (Veblen, 1975 [1899a], p.154).

The above quotation certainly reflects the aspect of Veblen’s thought that has strongly inspired neoclassical literature to furnish original interpretations of his theory. The already mentioned Veblen effect of Leibenstein (§ 2.2.1.1) is the main example of this.

While the author gives useful information about the features of luxury goods no particularity is given to the concept of wage goods. Here a wage good is simply identifiable as a good prevalently consumed by workers and with features different from luxury goods; in generic terms wage goods are identifiable as ‘basic’ goods. However, according to Fisk (1959, p.53) in his interpretation of Veblenian thought, a good is identifiable as a wage good if it is “directly conducive to the furtherance of human life” while a luxury good is simply an *embellished* wage good. Moreover, he adds that if a luxury good derives from the embellishment of a necessary good then - “on a continuum of products and services” (Fisk, 1959, p.53) – the luxury good becomes a necessity.

2.2 Income distribution

In the previous chapter it has been seen how the internal conflict of the firm can generate unemployment. On this point Veblen seems to maintain a consistent line of thought in most of his writings. It is more complicated however, to trace a possible Veblenian theory of economic growth and employment *via* the Veblenian theory of income distribution. More specifically, Veblen does not have a clear and precise theory of income distribution and the effects of a different income distribution on economic growth and employment can be both positive or negative for him. It will be argued how a distribution of income in favour of the leisure class can have a positive effect on the level of output and employment by the working of a virtuous process *via*

the increase of demand, production and employment. Moreover it will be shown that such a process is in fact a revaluation of the Malthusian effect of unproductive consumption and for this reason it can be called the *Malthusian element in Veblen*. At the same time it will be argued how a distribution of income in favour of the leisure class determines a reduction of output and unemployment *via* the increase of financing costs. Before examining such points let us try to order Veblen's thought on the composition of income and on its distribution. Recently Tilman (2003, p.xx) has remarked: "although [Veblen] never specifically articulated a theory of income distribution, his evolutionary view of social change suggests an unending process of adjusting means to ends, and ends to means, with community serviceability (social usefulness) as the standard of value for economic activity. Income should thus be distributed so as to facilitate the instrumentally adaptive efforts of society to achieve the generic ends of life as well as successfully cope with unending change". Tilman means that Veblen's theory of income distribution seems to follow a logic of natural selection, in other words income is naturally distributed amongst classes on the basis of their capacity of adaptation to environmental conditions. Apart from this interpretation, it is difficult to find comprehensive analytical reconstructions of Veblen's theory of income distribution in the contemporary literature. As has been said, Veblen does not build a specific theory of income distribution but a theory on this topic can be found in Veblen by the parallel reading – at least – of the following works: *a) The Theory of the leisure class*, *b) The Theory of Business Enterprise* and *c) On The Nature of Capital*, *d) The Engineers and the Price System*.

More specifically the Veblenian theory of income distribution has different traits: *a)* income distribution does not reflect the contribution to production of the production factor; so Veblen opposes the idea that "whatever yields an income is a productive factor"; *b)* incomes are assigned on the base of the social recognition of the social status of workers and they derive from ownership rights; on this point Veblen remarks that income is distributed merely on the basis of a *formal* and *institutional* recognition of participation of production factors in production; the formalization is a purely institutional matter and makes reference only to the legal possession of a production factor and not to its effective use. In these terms he does not think that "any legally defensible receipt of income is a sure sign of productive work done" (Veblen, 2001 [1921], p.21); he also remarks that an effective factor of production does not

concretely receive the due income if it lacks of the possibility of being owned. Finally *c)* the origin of categories of income – rents, profits and wages – is not economic but institutional. More specifically, rents originate in conspicuous consumption, profits in the institution of ownership and finally wages in ‘institutionalized’ subsistence. Let us see in more detail the economic categories of income in Veblen in the specific form of financial rents of the leisure class, profits of undertakers and the wages of technicians and workers.

2.2.1 *Financial rent as leisure class income*

With particular reference to the income of the leisure class, interpreting and expanding Veblen’s thought it is reasonable to think that the main source of income for the leisure class is rent in the specific form of financial rent⁴⁹. Financial rent is definable as

⁴⁹ Even though Veblen is not particularly interested in the analysis of land rent, he does not shy away from saying something on the topic. As he writes “rent is of the nature of a differential gain [...]. The differential advantage attaching to agricultural land [...] rests on certain broad peculiarities of the technological situation (Veblen, 1908a, p.529; italics added) [as well as] the preferential position of the landlord [which] consists in his legal right to decide whether, how far, and on what terms men shall put this technological scheme into effect in those features of it which involve the use of his parcel of land (Veblen, 1908a, p.530)”. From the above quotation it appears that Veblen does not add new interpretations of land rent as regards the classical interpretation. He only tries to expand his institutional theory of rent to land rent. Even if Veblen had little interest in the question of land rent the matter was not absent in the debate of his times. Note that the American agrarian policy mainly aimed at the transfer of land ownership into private hands to ensure a better use of it. In 1862 the Homestead Act for example granted 160 acres free to farmers whose only obligation was to cultivate the land for at least five years (see Cameron 1993 ch.12). Certainly the Homestead Act had positive effects on the distribution of land to the population with the intent to increase productivity and production but some economists were convinced that such a policy was not enough to guarantee development. The American economist Henry George for example in his “Progress and Poverty: An Inquiry into the Cause of Industrial Depressions and of Increase of Want with Increase of Wealth: The Remedy” (1879) also stresses the effectiveness of policies of taxation of land rent for the country’s development and economists (see for example Schumpeter, 1990 [1954], vol. III, p. 1063-1064) remember him mainly for his purpose of nationalising land rent. Land rent in fact is seen by George as part of wealth that does not serve to reproduce or increase the conditions of production of a land but mainly as part of wealth that is appropriated by a simple right – or rather a privilege – to the possession and use of the same land. As George writes: “rent or land value does not arise from the productiveness or utility of land. It represents in no wise any help or advantage given to production, but simply the power of securing a part of the results of production. No matter what are its capabilities, land can yield no rent and have no value until someone is willing to give labour or the results of labour for the privilege of using it; and what any one will thus give depends not upon the capacity of the land but upon its capacity as compared with that of land that can be had for nothing” (George, 1912 [1879], ch.8). If land rent is taxed production and productivity is not depressed since its taxation does not affect the land-input, as well as wages and capital but simply a right of landlords. Moreover, according to George, the higher the taxation of land rent, the higher the economic growth. As he writes “the whole value of land may be taken in taxation, and the effect will be to stimulate industry, to open new opportunities to capital, and to increase the production of wealth. [In fact] if land were taxed to anything near its rental value, no one could afford to hold land that he was not using; and consequently, land not in use would be thrown open to those who would use it. But the whole value of land may be taken in taxation, and the effect will be to stimulate industry, to open new opportunities to capital, and to increase the production of wealth” (George, 1912

the remuneration of money capital given on loan and can include: *a)* interest on banking loans, *b)* interest on bonds and *c)* dividends. In Veblen it is not the nature of a security that qualifies it as credit security or as representative security of registered capital, but who the owner is. In other words if stocks and bonds are owned by outsiders then these stocks and bonds are credit securities. In the same times if stocks are owned by insiders then stocks are representative securities of registered capital. Veblen does not specify who the outsiders and insiders are but it is reasonable to think that when he speaks about outsiders he is referring to external investors that place their own money at undertakers' disposal like members of the leisure class; in this case the leisure class has no interest in managing firms but just in having a money income. On the other hand insiders are those undertakers that own stocks with the purpose of effectively managing firms and having profits. Remember that the leisure class (see § 2.1) is assumed to control the monetary-financial market in the sense that in the monetary market it is able to fix the interest rate since it owns the right to the production of money whose supply depends on its demand expressed by firms. In the financial market members of the leisure class buy stocks and bonds. Here the leisure class can decide the quantity of stocks and bonds but not – at least directly – their remuneration. Dividends depend on the quantity of profits produced by firms while interest on bonds depends on the interest rate fixed by undertakers. However at the same time both the dividend rate and the interest rate on bonds necessarily have to be 'competitive' with the interest rate fixed in the monetary market. It is therefore possible to say that the leisure class in fact controls quantity and remuneration of money taken on loan both in the monetary and financial market because when the leisure class fixes the interest rate in the monetary market undertakers have to borrow a quantity of money at least sufficient to generate profits that are able to pay a dividend rate and an interest rate on bonds at least equal to the interest rate fixed on the monetary market. This is probably the implicit reason why the interest rate is a financing cost in Veblen. Along with interest on banking loans and interest on bonds, also dividends are financing costs since they are part of profits that undertakers have to give investors for their loan reducing the firms' possibility of self-financing.

[1879], ch.17). Moreover he adds (1912 [1879], ch.12): "unlike taxes upon commodities, or exchange, or capital, or any of the tools or processes of production, taxes levied upon the value of land do not bear upon production [...]. Taxes may be imposed upon the value of land until all rent is taken by the state, without reducing the wages of labour or the reward of capital one iota; without increasing the price of a single commodity, or making production in any way more difficult".

Moreover, since dividends, interest on banking loans and interest on bonds are all financing costs they are in fact a “charge”, a ‘bounty’ on profits. As he writes:

“Productive industry yields a margin of net product over cost, counting cost in terms of man power and material resources; and under the established rule of self-help and free bargaining as it works out in corporation finance, this margin of net product has come to rest upon productive industry as an overhead *charge payable to anonymous outsiders who own the corporation securities*” (Veblen, 1964 [1919a], p.48; italics added).

Then he adds

“The net product is the amount by which this actual production exceeds its own cost, as counted in terms of subsistence, and including the cost of the necessary mechanical equipment; this net product will then approximately coincide with the annual keep, the cost of maintenance and replacement, of the investors or owners of capitalised property who are not engaged in productive industry; and who are on this account sometimes spoken of as the “kept classes”. Indeed, it would seem that the number and average cost per capita of the kept classes, *communibus annis*, affords something of a rough measure of the net product habitually derived from the community's annual production” (Veblen, 1964 [1919a], pp.55-56).

Veblen does not build a precise theory of financial rents. A better understanding of his theory of interest – for example – can be traced by the connected reading of his theory of credit with his critiques of the Austrian and American theory of interest (see Veblen, 1892; 1908d; 1909b). As the author writes: “Interest is, strictly, a phenomenon of credit transaction alone. [It is a] business proposition [which] is to be explained only in terms of business” (Veblen, 1909b, p.299). In other words interest is simply the remuneration of financing investments aimed at the realization of monetary gains. So interest has no relation with the real productivity of capital or with the intertemporal choices of consumption. More specifically unlike Austrian and American school of capital (Böhm-Bawerk, Fisher, J.B. Clark), Veblen looks at interest as a “business proposition [explainable] only in terms of business” so he interprets interest as a “pecuniary phenomenon” (Veblen, 1909b, p.298) not as a real one. Consequently Veblen is far removed from the neoclassical interpretation of the nature of the interest rate. In fact he does not consider the interest rate the price of

waiting for “roundabout processes” as in Eugen von Böhm-Bawerk or the optimal rate of substitution of future income with the current one as in Irvin Fisher.

2.2.1.1 *On the nature of financial rent: conspicuous leisure*

In view of what has been said above, financial rent is definable as remuneration of the money capital given on loan. This gives rise to an important question: what does the origin of rent depend on? Rereading Veblen it is possible to say that the origin of financial rent is in the traits and working of the main activity of the leisure class, that is to say conspicuous leisure. This mainly means that the origin of financial rent is not economic but institutional. The leisure class is recognized by Veblen as a class continuously affected by an internal competition amongst its members for the reaching of the excellence of their own status. Such competition is played out through conspicuous consumption, in other words, on a consumption involving luxury goods ostentatiously displayed to others and for this reason also called “competitive consumption” or “waste” (see Veblen 1969 [1915], p.379). The ostentation of consumption is addressed to generating envy seen as a social tool for the acknowledgment of the pecuniary superiority of others. As Veblen writes:

“Customary expenditure must be classed under the head of waste in so far as the custom on which it rests is traceable to the habit of making an *invidious pecuniary comparison*” (Veblen, 1975 [1899a], p.100; italics added).

It is important to notice that Veblen speaks about envy in “a technical sense” (Veblen, 1975 [1899a], p.34). More specifically, Veblen considers envy as “process of valuation of persons in respect of worth” (Veblen, 1975 [1899a], p.34). In these terms he “[has no] intention to extol [it] or depreciate [it]” (Veblen, 1975 [1899a], p.34). Conspicuous consumption is therefore consumption driven by an institutional motive: obtaining social esteem *via* the mechanism of “invidious comparison”. In the Veblenian vision an individual is socially esteemed if s/he has a “conventional standard of wealth”. To obtain social esteem the same individual must takes steps to reach the conventional standard of wealth, and then display in order to be envied. If

the conspicuous consumption is envied then the individual has achieved his/her aim: social success. As Veblen writes:

“In order to stand well in the eyes of the community, it is necessary to come up to a certain, somewhat indefinite, conventional standard of wealth [...]. Those members of the community who fall short of this [...], suffer also in their own esteem, since the usual basis of self-respect is the respect accorded by one’s neighbours” (Veblen, 1975 [1899a], p.30).

In order to guarantee a given “conventional standard of wealth” members of the leisure class - owners of banks - fix an interest rate in the monetary market at least sufficient to cover their consumption⁵⁰. The additional way of guaranteeing the conventional standard of wealth is the purchase of stocks and bonds Veblen’s aim of constructing a theory of conspicuous consumption is mainly addressed to showing the serviceability of luxury goods for social well-being. As Veblen writes:

“The serviceability of goods for consumption has come to be the most *obtrusive element* of their value [as] honorific evidence of the owner’s prepotence” (Veblen, 1975 [1899a], p.24).

Hence Veblen uses the term waste as synonymous of competitive consumption and conspicuous consumption. With these terms – as in the concept of envy – Veblen does not mean to give value judgements to the concept; he merely wants to identify a particular kind of consumption rather than judging it (see Veblen, 1899b, pp.107-108). As he remarks:

“[Waste] is here used for want of a better term that will adequately describe the same range of motives and of phenomena, and it is not to be taken in an odious sense, as implying an illegitimate expenditure of human product or of human life” (Veblen 1975 [1899a], p.97).

So with the concept of waste he wants to maintain a neutral analysis for the purpose of showing its utility for social well-being. On this point he stresses:

⁵⁰ Veblen is unclear on the structure of the money market. One can argue that their structure is similar to the structure of the market for goods, so that banks work in a monopolistic competition environment. As a result, due to the low elasticity of the demand for money on the microeconomic plane, bankers are able to gain money revenues, i.e. financial rents, by means of interest rate increases.

“It is here called waste because the expenditure *does not serve* human life or human well-being *on the whole*, not because it is waste or misdirection of effort or expenditure as viewed from the standpoint of the individual consumer who chooses it” (Veblen, 1975 [1899a], pp.97-98; italics added).

In the above quotation Veblen argues that waste is not criticisable at a microeconomic level. From the micro point of view he calls the utility of consumption, which is subjective and not censurable, “relative utility” (Veblen, 1975 [1899a], p.98). He remarks that waste “has utility to [the individual] by virtue of his preference” (Veblen, 1975 [1899a], p.98) so it cannot imply “depreciation of the motives or of ends sought by the consumer under this canon of [...] waste” (Veblen, 1975 [1899a], p.98). On the other hand, on the macro plane he replaces the idea of relative utility with “the test of impersonal usefulness” (Veblen 1975 [1899a], p.98). So Veblen does not admit value judgements on an individual level as regards preferences; however the collectivity expresses value judgements when the sum of individual behaviours produces negative outcomes for the collectivity itself (see Veblen, 1899b, p.108). It could be argued that the implication is that the Veblenian individual is an agent who tends to state value judgements on economic variables. Accordingly, individuals would seem to see society not as an aggregation of individuals but as an autonomous and impersonal entity whose only reference for conduct is the human life of the whole, that is to say the “point of view of the generically human”. So from the point of view of society, waste “does not serve” collectivity since the use of social resources for “invidious [...] comparisons” limits “enhanc[ing] human life on the whole” (Veblen, 1975 [1899a], p.99). Actually Veblen does not clearly explain the effect of waste on social well-being. He confines himself to accepting and describing the effect of waste according to the conventional sense of waste for common man: the use of resources for futile motives (see also Bush, 1999, pp.136-137). On the macroeconomic plane Veblen clearly identifies four categories of waste, grouped by Rutherford (2001, p.175) into four main classes: “monopoly restrictions, business cycle, unemployment, and competitive advertising” even if the effective classes of waste are identified by Veblen in the following terms:

“(a) Unemployment of material resources, equipment and manpower, in whole or in part, deliberately or through ignorance; (b) Salesmanship (includes, e.g. needless multiplication of

merchants and shops, wholesale and retail, newspaper advertising and bill-board, sales-exhibits, sales-agents, fancy packages and labels, adulteration, multiplication of brands and proprietary articles); (c) Production (and sales-cost) of superfluities and spurious goods; (d) Systematic dislocation, sabotage and duplication, due in part to businesslike strategy, in part to businesslike ignorance of industrial requirements (includes, e.g. such things as cross-freights, monopolization of resources, withholding of facilities and information from business rivals whom it is thought wise to hinder or defeat)” (Veblen, 2001 [1921], p.68).

Historians have tried to investigate in more detail the topic of conspicuous consumption with particular reference to its methodological aspect and its effects. Some of this literature is critical of Veblen on the possibility that consumption is driven by macro choices rather than by micro choices (see for example Cummings, 1899; Flux, 1923; Mills, 1956; Leibenstein, 1950; Meek 1963; Hamilton, 1987; Campbell, 1995) while some supports the idea and tries to expand it in different ways (see for instance Edgell, 1992; 2001; Mason, 1995; Eby, 1998; Tilman, 2003; Forges Davanzati, 2006a). Generally speaking a controversial matter in literature – well raised by Campbell (1995) – regards the exact, commonly-agreed definition of conspicuous consumption. The definition of conspicuous consumption would seem to be simple but actually it is extremely complicated. By his theory on consumption Veblen – as Tilman (2003, p.xvi) remarks – identifies two kinds of parallel consumption: *a*) “conspicuous [and competitive] consumption”, and *b*) consumption “aimed at the satisfaction of functional and biological needs”. This is important for drawing attention to the fact that Veblen’s theory of consumption regards a particular kind of goods – luxury goods – and it is not applicable to all categories of goods and consumption. In other words he does not set out to analyse consumption in all its forms but only in one specific form.

On the concept of waste John Cummings raised his famous critique in the same year of publication of the *Theory of the leisure class*. The author particularly wants to critically debate the concept of waste on the macro plane. In particular he remarks that the Veblenian idea of society as an impersonal entity “is an imaginary and fictitious phantom which has no existence at all apart from the individual conceiving it” (Cummings, 1899, p.428); so “impersonal usefulness” cannot have any logic sense. According to Cummings what serves all individuals is equal to what each of them wants; so if waste is not criticisable at a micro level, it automatically cannot be

criticisable at the macroeconomic level either, since “enhanc[ing] human life on the whole” is the enhancing of all the single lives. Cummings feels waste in Veblenian terms is perfectly compatible with social well-being; in fact as he writes – in Cummings (1899, p.430) - “[the] invidious distinction comes to identify itself with the desire to live” in an excellent manner so an aggregate behaviour that follows such logic necessarily improves the human life on the whole.

Some years later Flux (1923) critiques Veblen’s intent to macro-found the theory of consumption stressing that conspicuous consumption is not an expression of competition amongst individuals so it has no institutional nature. Following Flux conspicuous consumption is – like other kinds of consumption – an expression of individual choice. More specifically, according to the author conspicuous consumption concretely represents the expression of the desire of each individual to go beyond the limit of “needs of existence” (Flux, 1923 [1904], pp.24-25). So interpreting Flux, the aim of an individual is maximizing the “desire for distinction” which is micro-founded by the increase in the consumption of luxury goods.

Leibenstein (1950) is not interested in investigating the internal consistency of the Veblenian theory of consumption. He tries to absorb the Veblenian theory of consumption into the neoclassical logic of consumption theory, concentrating on the possibility of building the demand function of goods in the presence of what the author himself calls the Veblen effect. In particular Leibenstein (1950, p.189) defines “the Veblen effect” in the following terms: “by the Veblen effect we refer to the phenomenon [for] which the demand for a consumer good is increased because it bears a higher rather than a lower price”. With the aim of building up the demand for goods subject to “conspicuous consumption” the author makes reference to two kinds of prices, namely: *a*) the “real price” and *b*) the “conspicuous price” (Leibenstein, 1950, p.203)⁵¹. As he writes “by the real price we refer to the price the consumer paid for the commodity in terms of money” (Leibenstein, 1950, p.203). On the other hand “the conspicuous price [is] the price that the consumer thinks other people think he paid for the commodity” (Leibenstein, 1950, p.203, footnote 1). Demand increases if the real price decreases and increases if conspicuous price increases. A reduction of

⁵¹ Alongside the “Veblen effect” Leibenstein (1950, p.189) adds two other external effects on the utility function: *a*) the “bandwagon effect” and *b*) the “snob effect”. As he writes: “by bandwagon effect we refer to the extent by which the demand for a commodity is *increased* due to the fact that others are also consuming the same commodity”, while “by snob effect we refer to the extent to which the demand for a consumers’ good is *decreased* owing the fact that others are also consuming the same commodity”.

real price of a good can produce an increase or a reduction of demand. This depends on the difference between the real price and the conspicuous price. In particular if real prices are higher than a given conspicuous price, demand for goods increases when real prices decrease – or rather demand increases in a less proportional manner. On the other hand, if real prices are lower than the given conspicuous price, demand decreases when real prices decrease – or rather demand decreases in a highly proportional manner. In the first case the price effect prevails while in the second case the Veblen effect prevails. So demand can be negatively inclined, positively inclined or “a mixture of both” (Leibenstein, 1950, p.204). The prevalence of one kind of inclination rather than another depends on the prevalence of one effect over the other; in other words if the price effect is higher than the Veblen effect, demand for goods will be negatively inclined; on the other hand, if the Veblen effect is higher than the price effect, the demand will be positively inclined. In 1996 Bagwell and Bernheim made a critique of Leibenstein’s model, arguing that the Veblen effect is a misunderstanding of the original vision of conspicuous consumption. In their interpretation demand for conspicuous goods is not a function of prices but a function of status, which is technically the informative signal of wealth also stressing that each “individual’s status depends upon perceptions of his wealth among social contacts” (Bagwell and Bernheim, 1996, p.351)⁵².

Apart from Leibenstein’s model, in those years the literature continued to analyse the internal consistence of the Veblenian theory of conspicuous consumption. Mills (1956) for example stresses that Veblen implicitly builds his theory on the bases of precise hypotheses: the perfect knowledge of the sense of honorific consumption and its stability. In other words individuals know *a priori* the aim of consumption, in terms of the prestige-goal, and they know that this goal is stable over time. But if individuals know *a priori* the prestige-goal and if such a goal is also stable then competing with others in consumption is not necessary. It is sufficient for the same individuals to autonomously build an individual consumption plan to achieve their goal. In this case the micro foundation of conspicuous consumption is maintained as in Flux. However Mills does not appear completely opposed to a macro foundation of

⁵² Cullison (1978) shows that conspicuous consumption is perfectly compatible with neoclassical methodology and that neoclassic economists – contemporaries of Veblen – failed to explain such consumption only because they did not consider the hypotheses of possible interdependence of consumer preferences. For a critique of the neoclassical approach to conspicuous consumption – based on the idea that mainstream “moral agnosticism” should be rejected – see Tilman (2006).

conspicuous consumption. As remarked by the author, Veblen's theory works if people do not have a clear idea of the meaning of prestige, honour, social status, etc., if this idea is so extremely relative and not objectively definable and also if this idea is not stable over time then people live in "an unstable system of prestige". If society is permeated by an unstable system of prestige then the competition with others to consume is possible. In other words, Mills argues the competitive consumption in Veblenian terms could naturally be induced from those conditions for which people do not exactly perceive the sense of honourableness. In this case each individual lives within an uncertain state – which Mills (1956, p.240) calls "the virtual status panic" – as regards the effective sense of honourableness, so they continuously consume simply because they trust in what others do, thinking that such consumption is meritorious. The social instability of the sense of prestige therefore becomes the sufficient condition for the setting up of continuous consumption among individuals as in Veblen for the search for a state of certainty about the sense of prestige. However since the individual lives in a continuous state of uncertainty, the reaching of a level of prestige is not the end of conspicuous consumption since society continually re-discusses the level itself, pushing individuals into the pursuit of the new level of prestige by fresh consumption.

In addition Meek (1963, p.317) critiques the idea that conspicuous consumption is consumption aimed at invidious comparison. The author remarks that conspicuous consumption is always an expression of social relationships and of the pursuit of social acceptance. Social acceptance works on friendly relations rather than on envy, i.e. on grudge relations. In fact Meek's interpretation is built considering invidious comparison – and therefore envy – in a non-technical sense as Veblen would like to do but with a common meaning as Veblen in fact does when he tries to explain the effect of waste.

The micro foundation of conspicuous consumption reappears in 1987 in the Hamilton model. The author points out that Veblen's conspicuous consumption – unlike other kinds of consumption – presents two main traits: the "ceremonial" and "the instrumental" trait. As the author writes "we use goods as symbol of status and simultaneously as instruments to achieve some end-in-view" (Hamilton, 1987, p.1541). In Hamilton's opinion, Veblen rightly builds his theory of conspicuous consumption assuming that the ceremonial utility of the good is surpassed by the

instrumental utility (cf. Merton, 1957). But if the instrumental utility surpasses the ceremonial utility then conspicuous consumption is no different from other kinds of consumption. In fact Hamilton believes that each kind of consumption works by a common rule: the “if-then context” rule (Hamilton, 1987, p.1548). To explain this rule he presents the *example of the wrench*. As he writes “*if* [...] my attention is focused on the removal of a series of hexagonal nuts of varying sizes [*then*] I [...] value an adjustable wrench. My *judgement* of its goodness is how *effectively* it functions in *conjunction* with my skilled use of it in removing the set of nuts. I do not choose a pipe wrench because it would score the heads and render unfit any kind of wrench for their removal in the future. *We judge according to present and future known consequences*” (Hamilton, 1987, pp. 1547-1548; italics added). So according to Hamilton conspicuous consumption is not institutionally derived and it is perfectly compatible with the rule of “if-then context”. It is therefore always subject to judgement as regards its consequences and depends: *a*) on knowledge of the objective features and on the functionality of a good and *b*) on knowledge of the subjective potentiality of utilization of the same goods. In turn the subjective potentiality of utilization supplies “style” which in fact – for Hamilton - is the “major symbol of status”. In conclusion with the Hamiltonian interpretation of conspicuous consumption it can be said that the status symbol is not the final point of the competition in consumption, it is the starting point of consumption which cannot be competitive since nobody would start a competition in consumption if s/he had no “style”, in other words *if s/he knew that s/he did not know how to consume*: the competition would in fact be already lost before starting. So competition is excluded *a priori* since status is not the aim of the consumption, it is a concretisation of a manner of consuming.

As seen above Veblen discusses conspicuous consumption in terms of motives and consequences. But according to Campbell (1995, p.37) Veblen fails to integrate them. First of all Campbell (1995, p.40) argues that: “conspicuous consumption is a form of conduct with two different sets of consequences: *a*) those [...] which have occurred in the attitudes and opinions of others, and *b*) those which the aspirant [...] consumer imagines have occurred”. Then Campbell argues that Veblen’s incapacity to integrate the motives with the consequences of conspicuous consumption invalidates his theory as “workable theory” (Campbell, 1995, p.37). What is lacking in Veblen – Campbell stresses – is the integration between his “two conceptual formulations”

which the author defines as “contrasting”. As he writes “these are first, an interpretative [...] version that conceives of conspicuous consumption as action marked by the presence of certain [...] motives, and second, a functionalist formulation in which conspicuous consumption is viewed as a form of behaviour characterized by particular [...] outcomes” (Campbell, 1995, p.37).

Eby (1998, p.692) tries instead to expand the theory of conspicuous consumption by investigating its relation with institutional change. In particular Eby stresses that conspicuous consumption is concretely an example of institutional inertia. As she writes: “conspicuous consumption encourages one to experience her life according to a particular temporal paradigm, as if life never ‘is’ but can only be experienced as ‘becoming’, by acquiring goods [s/he] desires but does not yet own”. Eby argues that conspicuous consumption could be considered a *stimulating and gratifying institution* for individuals and for this reason it is not subject to change. Concretely she remarks that the continuous stimulation and gratification - to which conspicuous consumption is subject and which does not affect the modification of the institution itself – depends on the fact that “a desired object does not [only] result in present satisfaction but [mainly] in the immediate desire for a new object” (Eby, 1998, p.692). The institutional inertia produced by conspicuous consumption is for Eby (1998, p.692) an outcome of “forward-looking thrust”. It is interesting to notice that Eby (1998, p.692) does not limit her analysis to conspicuous consumption as a self-sustaining process created by the leisure class but she extends it to the process nurtured by the firm’s activity, remarking that institutional inertia is not only generated by the leisure class but also by firms in advertising activities. The possibility that conspicuous consumption maintains institutional inertia is concretely present in Veblen. The leisure class – due to its typology and features of consumption – imposes decorous styles of living on the whole of society. As Veblen writes “[purchasing] is the need of conforming to established usage and of living up to the accredited of taste and reputability” (Veblen, 1975 [1899a], p.168). He also adds:

“The leisure class stands at the head of the social structure in point of reputability; and its manner of life and its standards of worth therefore afford the norm of reputability for the community. The observance of these standards, in some degree of approximation, becomes incumbent upon all classes lower in the scale” (Veblen, 1975 [1899a], p.84).

It is reasonable to think that the leisure class is not opposed to admitting the working class to luxury. If luxury is also accessible to the working class then it is more probable that institutional inertia will be maintained. On this point Edgell (1992, p.209) writes: “In fact Veblen claimed that the norm of conspicuous consumption is mandatory for all classes”. However because the working class lives at a subsistence level the accessibility to luxury is relative; it is relative for typology and cost of goods, it is only from the bottom towards the top and fundamentally it regards the next higher social classes⁵³. As Veblen remarks:

“The norm of reputation imposed by the upper class extends its coercive influence with but slight hindrance down through the social structure to the lowest strata. The result is that the members of each stratum accept as their ideal of decency the scheme of life in vogue in the *next higher stratum*, and bend their *energies* to live up to that ideal” (Veblen, 1975 [1899a], p.84; italics added).

So in view of this it is possible to notice that two kinds of emulative processes are present in Veblen: *a*) one *intra-group* (competitive consumption and certainly the most important for Veblen) and *b*) one *infra group* (accessible luxury) which is recognized by Tilman (2003, p.xvii) as competitive consumption like for the intra-group emulation competitively emulate the social strata *next* above them⁵⁴.

Modern literature has tried to furnish a rereading of the motives and effects of Veblenian waste. According to Edgell (2001, p.105) for example waste originates when consumption is in excess of the level which guarantees “reasonable physical comfort”. In “economic terms” – Edgell (1992, p.214) remarks – conspicuous consumption involves different kinds of waste: *a*) “conspicuous waste”- that is to say “loss of resources”, *b*) “conspicuous expense” – that is to say “poor economic value”

⁵³ This is the reason workers mainly consume wage goods as indicated in chapter 1.

⁵⁴ Bilkey in 1956 tested the hypothesis of the equitable income distribution upon consumption expenditure in particular upon conspicuous consumption expenditures between the 1920s and the 1950s in the United States. The aim of this study was to investigate the impact of a fair income distribution on the composition of consumption and on the process of infra group emulative consumption. The author starts from the following consideration: the emulative infra group consumption is the expression of income differences between the social classes since the upper class – without a conspicuous level of income – cannot have a particular standard of life and consequently it cannot impose models of consumption on the lower classes. Symmetrically – he adds – it should happen that when there is a fair income distribution emulative infra group consumption disappears. In fact his results confirm his hypothesis. Moreover, the author adds (1956, p.82): “an increase in the equality of income distribution (since it reduces the income disparity between the various socio-economic classes) [reduces] the social pressure on consumers to spend for conspicuous [...] consumption (such categories as clothing, transportation, personal appearance, shelter, etc.), and consequently results in an increased allocation to non-conspicuous categories (e.g. food). The reverse [occurs] when income become less equally distributed”.

and *c*) “conspicuous abstention from useful effort – that is to say “inhibited productive work”. Mason (1995, pp.871-872) supports Veblen’s original idea arguing that “conspicuous consumption” in Veblen’s vision is a “status-driven consumption” and it is not “utilitarian but social with individuals attempting to secure social status through consumption”.

Forges Davanzati (2006a, ch.3.) has recently tried to expand the theory of waste in the following terms: he argues that competitive consumption is identifiable as a game in which the final position for each consumer-competitor is equal to her/his own initial position but with a higher utilization of resources (like time, income, consumption, etc.) which – since his/her position has not changed – are in fact wasted. On the macroeconomic plane one could argue that waste limits social well-being due to three factors: *a*) because of waste in time and effort, part of the collectivity employs its time and effort in non-productive activities, *b*) since consumption of ‘wasteful’ goods is concentrated in the hands of a small part of the collectivity, *c*) because it is characterized by a continuous consumption of resources without limits or pause (see also Forges Davanzati, 2006b). On this point Veblen remarks:

“It is much more difficult to recede from a scale of expenditure once adapted than it is to extend the accustomed scale in response to an accession of wealth (Veblen, 1975 [1899a], p.102). [In addition] any retrogression from the standard of living which we are accustomed to regard as worthy in this respect is felt to be a grievous violation of our human dignity” (Veblen, 1975 [1899a], p.156).

As we have seen, the literature on conspicuous consumption has mainly concentrated on the internal consistency of Veblenian waste and little has been said instead about its effects. The last part of the present chapter and chapter 3 will present a rereading of conspicuous consumption in terms of its relation with financial rent with the aim of investigating its effects on economic growth and institutional change. However, it should be anticipated that a problem of internal inconsistency in Veblen has been identified since he is not so inflexible on the negative effects of waste for collectivity (see § 2.5).

2.2.2 *Profits and capital*

The Veblenian theory of profits and capital requires a preliminary observation on the nature of the firm. In Veblen's view, the firm is not a 'black box': it is an organization which exploits common knowledge via the existing property rights and which aims at obtaining money profits. Recently Viano (2003, p.354) has written: In "his mind firms [are] no more than bureaucratic and commercial structures that exploit[...] their formal ownership of raw materials and the means of production to unduly appropriate the stock of knowledge and competences that these embody". Even if the sense of Viano's considerations on Veblen's thought will be clearer in the course of treatment here the focal point is the firm/"formal ownership" relationship. Let us see why: Veblen formally looks at firms as a form of undertaker's investment whose traits have an institutional nature. Veblen sees the firm as a speculative matter connected to the institution of ownership (see Cutrona, 2005). As he writes:

"The ownership of the capital goods affords a discretionary power of misdirecting in the industrial process and perverting industrial efficiency, as well as inhibiting or curtailing industrial processes and their output, while the outcome may still be profitable to the owner of the capital goods" (Veblen, 1908b, p.108).

The firm is simply the object of the undertaker's pecuniary investment by which s/he acquires the right to use his/her ownership to increasing his/her pecuniary wealth. In other words firms are legitimate tools for the realization of monetary gains – profits – in favour of their owners. So investment is strictly linked to the ownership of wealth, and in turn, to the natural proclivity that has determined it: the predatory instinct. As will be explained more clearly below, the ways profits are made – as with the utilization of industrial capital – concretely have a predatory nature; when an undertaker obtains profits s/he concretely removes something from others at a higher level concerning a thing that may be transferred to them. Predatory instinct pushes the individual to act in such a way as to for have more and ownership represents the right to benefit from extraneous things. It could be argued that investment is a peculiar form of predatory act aimed at obtaining profit. On investments Veblen writes:

"Investment is a pecuniary transaction, and its aim is pecuniary gain. [...] Invested wealth is capital [...] measured in terms of value and determined [...] by a valuation which proceeds on an

appraisal of the gain expected from the ownership of this invested wealth” (Veblen, 1908b, pp.104-105; italics added).

So investment “represent[s] expected income-streams” (Veblen, 1908b, p.124); the firm is therefore the object of “the [capitalization of] prospective gain” (Veblen, 1964 [1919a], p.104). In the eyes of undertakers, the firm is merely a fund of value and its aim is to furnish new value. The main purpose of the firm is to change pecuniary expenditure into pecuniary gain, namely an “item of wealth” into an “income-stream”.

The main variable that can affect the investment by undertakers is the expectation of income-streams. The inverse relation between interest rate and investments holds in contexts where uncertainty does not exist, or, in other words, an increase in the interest rate reduces investments only insofar as entrepreneurs’ expectations are not significantly optimistic⁵⁵. On the role of expectations Veblen simply remarks:

“The market fluctuations in the amount of capital proceed on variations of confidence on the part of investors, on current belief as to the probable policy or tactics of the guild of politicians, and of the indeterminable, largely instinctive, shifting movements of public sentiment and apprehension. So that under modern conditions the magnitude of the business capital and its mutation from day to day are in great measure a question of folk psychology rather than of material fact” (Veblen, 1904, p.149)⁵⁶.

⁵⁵ The expectations are relevant in Veblen even if he does not spend as much time on the elaboration of a clear theory of expectations and uncertainty as John Maynard Keynes. It is interesting to notice that the comparison of Veblen’s theory with that of Keynes is not new in literature; at the same time such literature is not as numerous or as rich as the literature which has tried to compare Veblen with Marx. Actually many points of Keynesian theory can be found in Veblen, or it would be better to say that many points of Veblenian theory are traceable in Keynes; in fact Keynes started to publish his more important works after the 1920s, so five years after the publication of Veblen’s *Theory of Business Enterprise*, that is to say the main Veblen work on which a comparison with Keynes can find a concrete validity. Rutledge Vining in 1939 published the work entitled “*Suggestions of Keynes in The Writings of Veblen*” stressing that “much of Keynes’s theory of employment can be dug from Veblen’s institutions” (Vining, 1939, pp.692 ff.; see also Mouhammed, 2003): from “the notion of effective demand” to the “schedule of marginal efficiency of capital”; from “the rate of interest which is wholly pecuniary” to the “rate of investment [as function] of [expectations and of] rate of interest”; from “the increased national income in response to capital expenditure” to “the propensity to consume”.

⁵⁶ Veblen does not present a clear, organized theory of uncertainty either in neoclassical terms or in Knightian or Keynesian terms (see Knight, 1971 [1921]; Keynes 1973 [1937]). At the same time the author does not escape the persuasion to also offer an institutional interpretation of uncertainty. The topic is approached in particular in *The Theory of Business Enterprises* (1904) and in *The vested interest and the common man* (1919). Here Veblen clearly writes about “imponderable article[s]”. More specifically, he writes: “an imponderable is an article of make-believe which has become axiomatic by force of settled habit” (Veblen, 1964 [1919a], p.9). This quotation supplies some hints: First of all uncertainty seems to be a human outcome. In fact, it is an outcome of thought and action. Consequently uncertainty is not in the *real* state of things but in the states of thought. Imponderability does not mean

The above quotation gives rise to an important consideration: Investments mainly depend on expectations on future profits, expectations on government policy and on “movements of public sentiment and apprehension”^{57,58}. Even if the question is not

impossibility to know or to foresee. At the same time imponderability does not mean riskiness. Uncertainty in Veblen’s thought just means absence of subjective or objective evaluation towards which institutions can lead. Institutions supply regular and fixed lines of conduct and thought which assume the form of axioms. In a static condition of an institutional order uncertainty becomes the rule since imponderability is actually in the state of things (see also Jennings and Waller, 1994, p.1016). In brief uncertainty seems to be a human limit, not a limit of the reality of things. In view of this, imponderability does not mean impossibility or limitation on knowing; rather it is a particular way of knowing facts; it is a way based on the role of institutions rather than on individualistic an rational calculus. It could be argued that uncertainty becomes a particular form of knowledge itself, a knowledge based on beliefs and actions which acquire the figure of axiomatic principles and where the axiomaticity is intended in a relative sense. In fact it regards principles and actions *conventionally* accepted: This is the reason why they do not need evaluation. If uncertainty works following the logic presented above then it could be added that uncertainty is first of all a feature of institutional inertia: in fact institutional inertia limits the ponderability of thought and action. In a dynamic process of institutional change the axioms in fact change and uncertainty changes form. However this does not mean that institutional change leads to certainty because ponderability is just momentary. In conclusion, in Veblen’s view, uncertainty is never eliminable since it is the cause-effect of institutions both in the static and dynamic condition of an institutional order. The above considerations may lead us to ask whether such a theory can be compared with the theory of Keynes. Actually there are at least two points of convergence of the two theories: *a*) uncertainty is in the state of things, and *b*) uncertainty cannot be removed. However the meaning of the state of things is different in the two authors as well as the reasons for which the condition cannot be removed. As Keynes writes in *The end of laissez-faire* in 1926 “[...] many of the greatest economic evils of our time are the fruits of risk, uncertainty, ignorance” (Keynes 1971 [1926], p. 291). In particular, according to the author, uncertainty is a completely different phenomenon from risk, in the sense that, given an uncertain event, no simulation tool is completely effective because of the intrinsic nature of the events themselves, or simply because the actual occurrence of some events depends on some modality that we cannot know (see also King 2002, ch.9). In fact, as Keynes writes: “[...] by uncertain[ty] I do not mean merely to distinguish what is known for certain from what is only probable. The game of roulette is not subject in this sense to uncertainty [...]. The sense in which I am using the term is that in which the prospect of a European war is uncertain, or the price of copper and the rate of interest twenty years hence, or the obsolescence of a new invention, or the position of private wealth owners in the social system in 1970. About these matters there is no scientific basis on which to form any calculable probability whatever: we simply do not know it (Keynes 1973 [1937], pp. 113-114)”. The Keynesian definition of uncertainty has a deep-seated characteristic: the problem of uncertainty concerns the impossibility of forming knowledge about something before the thing itself occurs (see Keynes, 1973 [1921], p.3, p.19). If knowledge cannot be formed before acting a problem arises: upon what does a decision to act depend? Keynes gives particular emphasis to the role of expectations stressing that “the state of [...] expectation, upon which our decisions are based, does not depend [only] on the most probable forecast we can make. It also depends on the *confidence* with which we make this forecast (Keynes 1973 [1936b], p. 148; italics added; see also Keynes, 1973 [1936a], 1973 [1936b], 1973 [1937], 1973)”. The literature on Keynesian uncertainty is extremely varied and although this is not the place for a complete review of it, recommended works are, amongst others: Kregel (1987), O’Donnell (1991). Runde (1991), Dequech (1997, 1998, 1999), Ferrari Filho (2001), Pacella (2006b).

⁵⁷ On this point it is interesting also to consider this quotation in the *Theory of Business Enterprise* (ch.4): “notoriously, business men are jealous of any attempt to change the value or lessen the stability of the money unit, which goes to show how essential a principle of business traffic is the putative invariability of the money unit”. Here it is possible to notice that Veblen recognizes monetary stability as an additional requisite of investments. It has been seen in the previous sections that undertakers act to maintain high prices, but at the same time this quotation allows us to say that undertakers oppose monetary policies that can induce increased prices which the undertakers themselves do not want if demand decreases. In other words undertakers oppose exogenous processes of price increases since this can have a negative effect on the level of demand, and for this reason undertakers call for monetary stability.

clearly followed through by Veblen it is interesting to notice that in his vision uncertainty does not permeate – at least at the same level – all social classes. Uncertainty would seem a typical trait of undertakers and the association of the “magnitude of business capital” as “question of folk psychology” would support this thesis. Probably the attribution of uncertainty prevalently to the undertaking class is not incidental in Veblen; economic-historical events from the late 1860s to the early 1900s could have inspired Veblen in assigning uncertainty to the undertaking class. In fact in these years America experienced its impressive industrial revolution with continuous processes of industrial and economic change which made undertakers live in a constant state of uncertainty about the profitability of their investments.

Given the above premises let us see more in detail the relationship between *profits and capital*. According to Hopkins (1933), Veblen – like other American economists since the 1860s such as Frances Walker (1883), Frederick Hawley (1890), John Bates Clark (1892) and Frank Knight (1921) – structures a theory of profit with an intent common to the above economists, that is to say to propose different theories of profit in opposition to a common theoretical background: the theory of profit of John Stuart Mill. In fact all the above economists rejected Mill’s idea of profit as income composed by interest, wages of management, and the prize for the riskiness of the investment⁵⁹. Some of them separate interest from profit. In those years for example Walker made a distinction between capitalists and entrepreneurs; the income for the use of capital is the interest – determined in the capital market – and goes to capitalists while entrepreneurs obtain profits by the Ricardian rent principle. Consequently profit becomes an expression of the entrepreneur’s efficiency. In other words, profit is quantifiable as the wage of alternative employment payable to the least efficient entrepreneur. On the other hand Hawley argues that profit is simply the prize for the risks entailed by the investment and which cannot be externalised; so from profit he removes interest and the wage of the entrepreneur’s work. John Bates Clark

⁵⁸ The Veblenian idea of investment is next the Keynesian theory of investment. Here it is sufficient to make reference to the following quotation from Keynes to point out a common vision between the two authors. Keynes writes in the *Treatise on Money*: “Upon what does the demand price of capital goods depend? It depends on two things: on the estimated net *prospective* yield from fixed capital (estimated by the opinion of the market after such allowance as they choose to make for the uncertainty of anticipation) measured in money, and on the rate of interest at which this future yield is capitalised. [...] It follows that the price of such goods can change for either of two reasons, because the *prospective* yield has changed or because the rate of interest has changed” (Keynes 1971 [1930], pp.180-181; italics added).

⁵⁹ In these terms Mill quantifies profit; however the nature of profit is the abstinence from consumption, which finds its materialization in the capital advanced to the production (see Gootzeit, 1995).

instead builds a theory of profit assuming that profit is not a matter of interest or of the entrepreneur's wage or of a prize for risk; so no element of Mill's original theory of profit is retained by him. In his vision profit is a matter of productivity and input costs; analytically the firm maximizes profit when marginal productivity of inputs (labour and capital) is equal to their marginal cost (wages and interests). More specifically, Clark sees labour productivity as depending on the entity of capital, and the productivity of capital as the residual of labour productivity. In other words the effective productivity of all workers – and consequently their wage – is equal to the productivity of the last employed worker; this is due to the fact that the sum of outcomes realized by the preceding workers is not an expression of productivity of labour but of capital. When Clark looks at profit he is looking at the profit of the firm; in other words profit is a firm's outcome which is absorbed both by entrepreneurs and workers. This phenomena is evident in a dynamic context since in the static one the entrepreneur has the right to profit – calculated as the residual between revenues and costs – since s/he is the owner of saleable commodities; but in the dynamic context profit is reinvested by the entrepreneur in capital, and the increase of capital increases the worker wage bill since an increase in capital in fact increases the labour productivity of the last worker, and therefore of all workers at the same level, and consequently the wage bill increases at the same level for all workers⁶⁰. On the other hand, Knight argues that profit must be understood as the guarantee of entrepreneurs for their liability connected to negative and unexpected events. According to the author, risk is a calculable factor since it is connected to expected adversities whose costs can be transferred to others; on the other hand, profit – which is expressed as a residual of income – covers the cost of the non-expected or unforeseeable adversities (uncertainties) which are not calculable and cannot be transferred to others.

In contrast with the above theories Veblen puts forward a theory of profits connected to the capitalization of firms and technically Veblen defines capital as the capitalization of expected profits (see Veblen, 1904, ch. 5) speaking about “items of capitalized wealth” (Veblen, 1908b, p.124). It is interesting to note that a characteristic of profit is the institutional use of the capital. Given the same capital, different profit

⁶⁰ It is important to notice that Clark builds his theory using a precise assumption: the ‘reshuffling’ of workers; this means that the order in which workers enter and are employed in the production process is not relevant. As Clark writes “if the first unit of labour claims more than the amount [of the last one] employers will let him withdraw and will substitute for it the last unit” (Clark, 1965 [1899], ch.XII). On this particular point see also Robinson (1934) and Samuelson (1962).

levels and features are possible if the ways of using the same capital change. In Veblen the ways of capital utilization are institutional. In these terms the institution of ownership leads capital towards one kind of capital utilization while the institution of industry leads capital towards another kind of utilization. In the first case the utilization of capital is for monetary profit, in the second case it is for real profit. Hence the concept of profit is first of all an institutional concept and historically contextualized. As he writes:

“The concept of capital is, substantially, a *habit of thought* of the *men engaged in business*, more or less closely defined in practice by the consensus of usage in the business community” (Veblen, 1908e, p.113; italics added).

In addition since capital has an institutional origin then its meaning is historically contextualized. As he remarks:

“[The term of capital] does not remain the same from generation to generation; and it cannot, *at least as regards present usage*, be identified and defined by physical marks. [Then he adds] “Capital” in the usage of current business, undoubtedly has not precisely the same meaning as it had in the corresponding usage of half a century ago; and it is safe to say that it will not retain its present meaning, unimpaired and unimproved, in the usage of ten years hence” (Veblen, 1908e, p.114; italics added).

Note that Veblen’s theory of capital is different from those presented by Eugen von Böhm-Bawerk in 1884 and 1889 in his volumes of *Kapital un Kapitalzins*, and by Irvin Fisher in his 1906 work *The Nature of Capital and Income* and in *The Rate of Interest: Its nature, Determination and Relation to Economic Phenomena* of 1908. Veblen is also critical towards John Bates Clark and his *The Distribution of Wealth* published in 1899. Veblen builds his theory on capital during the first decade of the 1900s and the above works certainly provided him with interesting hints for sustaining his own ideas (see Veblen, 1892; 1908d, 1908e, 1909b). While Böhm-Bawerk identifies capital as a “roundabout process” – that is to say as productive input formed by a given quantity and time of utilization of work and raw materials employed in its production in the past – Fisher sees it as a fund of real wealth owned by each individual, where the real wealth is intended as a totality of real owned goods. So differently from Böhm-Bawerk, Fisher does not look at capital just in terms of

industrial equipment, and he does not see capital just as a matter for undertakers. However it can be said that of all of them, the theory that interests Veblen the most is that of John Bates Clark since it divides the concept of capital from the concept of capital-goods; in Veblen's vision these terms are "conceptually distinct, though substantially identical" in Clark (Veblen, 1908d, p.162). Clark regards capital as a fund of productive goods with capital-goods as the single component of this fund. In Clark's idea, capital is a system of productive goods - that is to say as industrial system - whose value is different - but not independent - from the sum of values of the single components. Veblen interprets the meaning of capital in Clark in the following way:

"Mr. Clark's conception of capital, should be the generalization that industrial capital - capital considered as a productive agent - is substantially a *capitalization of technological expedients*, and that a given capital invested in industrial equipment is measured by the portion of technological expedients whose usufruct the investment appropriates" (Veblen, 1908d, p.166; italics added).

Moreover the value of capital in Clark maintains its relationship of productivity with its single components, so the matter of its monetary valuation is irrelevant. As we have seen, the concept of capital is wider than the concept of capital goods and the transferring of capital is different from the transferring of capital goods. In the first case the object transferred is a complex production system while in the second case the object is just a mechanical good. In fact the transferring of capital is equal to a change of investment while the transferring of a capital good is simply the substitution of a physical thing. Consequently while the transferring of capital goods can be done without transferring capital, the transferring of capital cannot be done without the transferring of capital goods since while capital is necessarily made by capital goods, capital goods do not necessarily make capital.

More specifically, the relationship that Veblen shows between capital and profits is quantitative in the sense that the higher the investment, the higher the profits. Veblen tries to explain why this happens in the *Theory of Business Enterprise* (1904) arguing that the higher the capitalization, the higher the turnover and the lower the capital rotation, so the higher the profits. In particular Veblen assumes the turnover as the product of the speed of capital rotation by the capital where capital is equal to the sum of private capital plus a fraction of it which represents credit. Consequently the

capital rotation time is expressed as fraction between capital and turnover. Given the private capital an increase of credit determines an increase of turnover and the capital/turnover ratio decreases. Veblen (1904, ch.5) uses the following equation to

express the turnover: $T = \frac{1}{t} \left(c + \frac{c}{n} \right)$ ⁶¹. Apart from this analysis, in the *Theory of*

Business Enterprise Veblen does not clearly explain the economic reasons that allow the firm with a high level of capitalization to gain more. Some answers can be traced in his “Credit and Prices” (1905). Here Veblen finds several reasons why firms act in favour of new capitalizations by increasing their size and Veblen calls this tendency “speculative advance” (Veblen, 1905, p.461) since their enlargement is motivated by the aim to make more money profits⁶². Veblen specifically makes reference to three reasons stressing that:

“[the] presumed greater earning capacity of the corporations [...] may be due to economies of production, superior management, economies of sale, or what not” (Veblen, 1905, p.463).

In fact Veblen is implicitly assuming that the earning capacity of firms increases when they increase their size thanks to the achievement of monopolistic positions on the market which are presumably positions of natural monopolies, that is to say what he calls “efficient monopoly” (Veblen, 1905, p.464). As he writes:

“Price changes [...] will probably be regarded as the *effects* of monopoly rather than of the credit transactions which *initiate* the monopoly” (Veblen, 1905, p.463; italics added).

It therefore seems that the pursuit of larger sizes increases demand for money because of the presumed reaching of scale economies which allow the firm to increase its volume of business and thus its profits. Apart for the possibility for firms to reach natural monopolistic positions, a larger size allows firms to reach monopolistic positions and this is thanks to the investment in “tangible and intangible assets” (see

⁶¹ with 1= the time taken as reference (year, month, days, etc.), c = private capital, c/n = fraction of private capital taken in credit form, T = turnover. If we consider 12 months as time of reference we can write $T = (12/t)(c + c/n)$ and the time of rotation of capital becomes $t = ((c + c/n)/T) * 12$.

⁶² On the phenomenon of the firm’s capitalization Rutherford (1980, p.437) stresses that the distinction “between large corporations with market power [favoured by addition capitalizations] and small undertakings such as independent farmers” is a key feature of Veblen’s picture of profit in the capitalistic economies.

below). In fact Veblen then goes into detail of the kind of investment that firms can make with new capitalizations⁶³. On this point he mainly makes reference to the following kinds of investments: *a*) mechanical equipment, what Veblen calls “tangible assets” or “capital goods” or industrial capital and *b*) the immaterial capital, what Veblen calls “intangible assets” (see Veblen, 1908b, p.105). Tangible and intangible assets represent the capital owned by undertakers on which Veblen spends a considerable part of his study (see also McCormick, 1989). Hence he makes a difference between profit generated by the ownership of tangible assets and profit generated by ownership of intangible assets. Let us see the two points in more detail with a necessary comment: both intangible capital and industrial capital generate profits *via* economic and institutional sources.

a) Intangible capital. “Intangible assets are immaterial items of wealth” (Veblen, 1908b, p.105) that is to say immaterial goods – like patent rights, monopolistic control, advertising, brands, business signs, licences, benefits,

⁶³ It is important to notice that Veblen gives particular emphasis to the role of capitalisation also for the economic cycle. In his view, the economic cycle first involves monetary values – monetary capital and prices – and after this it becomes a matter of industrial production (see Veblen, 1904, ch.7). In addition the economic cycle is endogenously determined by undertakers via the blockage and expansion of production. The upward phase of the cycle is characterized by: *a*) capitalisation, *b*) high prices and *c*) free selling. On the other hand the downward phase is characterized by: *a*) low prices, *c*) forced sales and *d*) contractions of capitalisations (see Veblen, 1904, ch.7). Positive expectations of monetary profits generate expansive phases *via* the enlargement of capitalisation (*creation of credit*). With the use of new capital undertakers increase demand for capital goods; employment increases and production rises; income increases and demand for goods increases too; *sales* become *free* during this phase for Veblen in the sense that demand is fully satisfied by the increase in production. The effect of the enlargement of capitalisation is the increase in turnover and reduction of capital rotation time, so profits increase. The firm’s earning capacity thus increases and consequently the market value of the “business property submitted as collateral” rises (see Veblen, 1905, p.462). If the value of collateral increases, new capital can be created and firms obtain an *expansion of capitalization*. The higher the value of the firm’s capital, the less the firm’s creditors perceive a loss (see Veblen, 1904, ch.7). So the working of the system in the above structure leads creditors to imprudently examine the possibility of getting their money back (see Veblen, 1904, ch.7) and pushed by positive expectations they continue to supply new capital. In view of this, the new capitalisation appears to be the effect of a price increase, just as prices appear to be the cause of the first capitalisation, or as Veblen argues credit and prices “are mutually related as cause and effect” (Veblen, 1905, p.461). The expansive phase is therefore characterized by an inflationary process that affects both the price of capital and the prices of goods; however the system cannot absorb such a process for long for two main reasons: *a*) the price of capital exceeds the effective possibility of profit, *b*) and the prices no longer maintain their profitability. So in a given point of the cycle the system starts to produce “in excess of what the market will carry off at a sufficient profitable price” (Veblen, 2001 [1921], p.8), and consequently there is a crisis with the concomitance of the phenomena of overproduction. As a consequence the system changes its tendency: profits decrease; the reduction of profits – and the presence of any losses – push undertakers to reduce investments and to increase the number of dismissals; the reduction of profit determines an increase in unemployment as well as a reduction of capital value and consequently the risk of insolvency increases (*contraction of capitalization*). Creditors are less inclined to renew their own credit and they quicken the time of liquidation of credits discounting them with the bank (*liquidation of credits*). In addition the reduction of profits - or the presence of losses - pushes firms to sell their own products at lower prices with the aim of recovering money and squaring their own debts; Veblen calls the sale of products at undesired prices *forced sales*.

copyrights, etc needed for the setting up of a firm and useful since they are “pecuniarily serviceable” to undertakers (Veblen, 1908b, p.105). Intangible assets in fact are not useful for the collectivity since they cannot produce real goods so they are useful only for the owner (see Veblen, 1904, ch.6) since they reduce the degree of competition amongst firms and produce a differential of profits. They have an institutional character since they are products of “use and wont, law and custom” (Veblen, 1908b, p.112) and they have a value proportional to their capacity to control, manage and develop the profit differential; their institutional trait is more marked in their capacity of creation and consolidation of powers, ‘rights’, etc. *via* the “capitaliz[ation] [of] habits of life [like] habits, propensities, beliefs, aspirations, necessities” – *institutional sources* (Veblen, 1908b, p.116; p.123). Let us look for a moment at advertising. Advertising is an intangible asset whose aim is that of “diverting credulous customers from one seller to another” (Veblen 1964 [1919a], p.95; see also Veblen 2001 [1921], p.70). So advertising is a source of continuous conditioning – and for this reason a source of capitalization – of consumer habits towards goods and services of one firm rather than another. Consequently intangible assets “represent assured income which can not be assigned to any specific material factor as its productive source” (Veblen, 1964 [1919a], p.69) and they assure the right to obtain a differential gain as regards their own competitors and for this reason they are institutional forms of profit (see Veblen, 1904, ch.6). Actually Veblen is particularly interested in the analysis of advertising as a peculiar kind of intangible asset (see Veblen, 1904, ch.3). Veblen sees advertising in terms of business technique of a speculative kind aimed at the acquisition of differential profits on the market to the competitor’s detriment. This acquisition is not the result of action by firms on the technological side but on the business side. More specifically, Veblen configures advertising as the main technique of persuasion to purchase. It is mainly based on psychological and communicative techniques. Veblen opposes the idea that sees advertising as informative tool, since the purpose of advertising is not to inform but rather to convince. Consequently it does not set out to reduce the information gap between consumer and firm; so its purpose is not to help the consumer make a rational choice. It could be argued that not being an information tool, advertising does not act as an auxiliary tool to the decisional autonomy of consumers but in fact appears to be a tool aimed at the handling of the consumer and at the control of his/her decisional

autonomy. So advertising works by predefining and maintaining consumers' choices and, according to the author, the effectiveness of advertising depends on the ability of firms to construct a product image in line with "the points of view" of the consumers, in other words in line with his/her habits of thought. The higher the convergence between communicative image of the product and consumers' habits of thought, the higher the automatism of purchase (see Veblen, 1904, ch.3 footnote 20). Veblen classifies advertising in a two ways: *a*) competitive advertising, *b*) monopolistic advertising. The first kind of advertising is addressed to a virtual differentiation of products for the purpose of making products less replaceable, and therefore facilitating the formation of "differential monopolies". Instead the second kind is a consequence of the first one; firms use it with the aim of consolidating their positional advantage by the consolidation or amplification of their own market (see Veblen, 1904, ch.3). Advertising investment serves to create and maintain a consolidated state of trust between consumers and therefore to reduce the degree of replacement of the product and have more chance of raising prices. The Veblenian theory of "intangible assets" has been used by the literature in proposing an interpretation of a possible market model on the lines of Veblen's idea. Sweezy (1957) and then Arrow (1975) stress that Veblen indirectly thinks of monopolistic competition. As Arrow (1975, p.7) writes "Veblen puts great stress on product differentiation as an economic strategy and recognizes that trademarks, brand loyalty, advertising and other selling costs are significant elements of competition. These expenditures [are seen by him] as waste; they yield indeed a competitive advantage but no social advantage". Interpreting Veblen and as also remarked by Arrow, the investment in intangible capital – in particular in advertising activities – is a form a waste for the collectivity. Even though Veblen is not clear on this point, the concept of waste could be extended from the leisure class to undertakers. Let us see why: Advertising investment is in fact used to reduce competition, but continuous investments in advertisings first began from undertakers' competition to reduce competition. In other words in order to reduce competition undertakers compete with other undertakers on the level of advertising, spending large part of their resources in this area. So undertakers contend for consumers by increasing advertising investment, in other words by simple communication costs and image costs. In Veblen's thought such costs represent waste for the collectivity. Expanding interpretations on the theory of waste for the leisure

class it is also possible to see the waste of advertising both at a microeconomic and a macroeconomic plane. As in waste in consumption, undertakers' struggle to excel – the reaching of higher profits – is triggered by their investment in advertising which determines a final position for each competitor equal to his/her own initial position but with a higher utilization of resources, mainly money capital. Not having modified his/her position, the use of money capital is in fact wasted. On the other hand on the macroeconomic plane the waste is triple: *a)* firms invest in a virtual capital rather than in industrial capital; *b)* workers are moved from industrial sectors towards non-industrial sectors, principally in commercial activities and intermediation *c)* advertising supplies just one form of utility: the saleableness of the product; so it furnishes utility only to the undertaker but not to the consumer since it is an additional cost without an additional benefit for the consumer and in this way it simply reduces the purchasing power of the consumer via a due price increase (cf. Forges Davanzati, 2006a, ch.3). Although Veblen includes commercial intermediation in the category of waste activities he does not want to assume intermediation as complex of activities that necessarily produce waste. In other words commercial intermediation produces waste only if it is used for competitive selling independently from the network of product distribution to which it makes reference (see Veblen, 1904, ch.3). Steiner (1976, p.3) criticizes Veblen's theory on advertising, arguing that "Veblen does not entertain the idea that [this] marketing [input] might increase purchasing power by generating an increase in output". According to Steiner (1976, p.11) Veblen assumes that material productivity is just a technical matter and marketing activities cannot increase output; consequently, in Veblen, employment depends on industrial production and not on commercial activities. On the contrary Steiner argues that marketing activities reduce prices and increase output at least for two reasons: *a)* they "bring[...] the manufacturer economies of scale by enlargement of the market", *b)* they increase the efficiency of the distribution process by reducing trade mark-ups and retail prices and therefore increasing consumption and production.

b) Industrial capital. Let us remember that undertakers invest with the aim of obtaining monetary profits, so also industrial capital must be used for such purpose. In fact when undertakers look at capital goods they are looking at tangible assets which are "pecuniarily serviceable" to the owner (Veblen, 1908b, p.105). Tangible assets generate profits through their degree of utilization and turnover. More specifically a

way of obtaining high profits is to reduce the duration of the process involving the production of the profit. If profits depend on the reduction of capital rotation time then undertakers must find some ploy for reducing this time. More specifically, the reduction of this time depends on the increase of turnover and to increase the turnover undertakers rely on different tools such as *a)* business activities like advertising, and *b)* the employment of advanced industrial processes (see Veblen, 1904, ch.5). Technicians are therefore important for undertakers since their activity helps to find new technical solutions for increasing the turnover. However the level of technological development wanted by undertakers may not necessarily be equal to that desired by technicians; undertakers in fact aim at the introduction of new technology when it appears to be advantageous in terms of expected profit, while technicians aim at an introduction of technology under the non-bankruptcy condition. The reduction of turnover, due to technical improvements, allows the individual firm to increase its revenues, and – given the costs – the firm will exploit the technical improvements until the maximum exploitation of technical knowledge is reached.

2.2.3 *The institutional basis of the subsistence wage*

Differently from profits and rent Veblen does not consistently discuss the issue of wages. However, his writings can be seen to argue that workers are paid by a monetary wage that may - or may not - be in line with the subsistence wage. Probably Veblen's best work in which some general considerations on wages can be found is *Böhm-Bawerk's Definition of Capital and The Source of Wages*" (1892). The trigger for his analysis came from the wages-fund doctrine, not in its original version by John Stuart Mill in his *Principles of Political Economy* (1848) but mainly in Böhm-Bawerk's subsequent reconsideration for his theory of capital.

According to the wages-fund theory, the source of wages is real capital. It would be more accurate to say that according to this theory, the wage bill paid to workers is a fixed fund of wage goods at the starting period of production and its size is equal to the surplus resulting from the previous period of production. Consequently the wage is simply equal to the capital/workers ratio⁶⁴. Veblen agrees with the wages-

⁶⁴ Forges Davanzati (2002) has summarized the internal inconsistencies of the wages-fund doctrine. As stressed by the author the wages-fund doctrine can give rise to a paradoxical result. As he writes (2002,

fund theory as regards the idea that wages are paid in advance – since he rules out the possibility that workers have savings to use for their consumption – but he does not think that wages are advanced in real terms, but in monetary ones by the monetary capital of firm. In addition since the wage is paid in advance it cannot be paid by the product and no meritocratic criteria enter the logic of determination and awarding of wages. Consequently in Veblen’s thought it is clear that: *a)* wages are paid in advance, *b)* wages are anticipated by monetary capital, *c)* wages are not paid by the product of the labour force⁶⁵.

In addition through Veblen’s writings it is possible to investigate the process of wage determination. More in detail, in Veblen the process of wage definition is subject to atomistic bargaining in the absence of regulation and given an institutional level of real subsistence wage, i.e. a subsistence wage shared by the community and known by workers and undertakers when they bargain for the monetary wage. As he remarks:

“Wage is a fact incident to the relation of employer and employed. It is [...] fixed by *colloquial use*, an economic category whose scope is entirely within the *theory of production* as carried on by the method based on that relation” (Veblen, 1892; italics added).

In Veblen’s vision, the subsistence wage – in real terms – is given *on the institutional plane*, i.e. it is derived from the standard (or desired) habits of life. Since workers and

p.465): “when an excess of labour supply occurs, the average real wage tends to decrease because of competition among workers, and as a result, the wage bill drops below the wages-fund. Consequently the wages-fund would be fixed and variable at the same time”.

⁶⁵ As a consequence, the wage is not paid in relation to some kind of productivity. However it is important to notice that Veblen himself seems to accept the criterion of productivity-wage even if limited to the field of commercial intermediation. On this point he writes “the gains from these employments must plainly be accounted for on other grounds than their productivity, since they need have no productivity (Veblen, 1961 [1901], p.303). [In particular] since the ground of payment of wages is the vendibility of the product [...] it follows that wherever the difference in vendibility rests on a difference in the magnitude of the product alone, there wages should be somewhat in proportion to the magnitude of the product” (Veblen, 1961 [1901], p.304, footnote n.9). From the above quotations it can be concluded that *a)* commercial activities “have no productivity” because they do not produce real goods or services, *b)* any remuneration is paid as a function of the “vendibility of the product”; but in fact this should require a recognition of efficiency in commercial activity. However the same author writes: “it might, therefore, be feasible to set up a theory to the effect that wages are competitively proportioned to the vendibility of the product; but there is no cogent ground for saying that the wages in any department of industry, under a business régime, are proportioned to the utility which the output has to any one else than the employer who sells it. When it is further taken into account that the vendibility of the product in very many lines of production depends chiefly on the wastefulness of the goods [...], the divergence between the usefulness of the work and the wages paid for it seems wide enough to throw the whole question of an equivalence between work and pay out of theoretical consideration” (Veblen, 1904, ch.3, footnote 27).

firms bargain over the *money* wages, the equality between the exogenous subsistence wage and the current real wage is not ensured by endogenous market mechanisms. The equality of the real wage with the real subsistence wage is just incidental, or – as shown in § 3.3c – it can be guaranteed by social conflicts. Veblen writes:

“In the *ideal case* [...] the output of production should be held to such a volume that the resulting price of the limited output will take up the entire purchasing power of the underlying population, at the same time that *the livelihood which the owners allow their working force of technicians and workmen is held down to the “subsistence minimum”* (Veblen, 1967 [1923], p.67; italics added).

So the subsistence wage is conceived by Veblen in real terms and has an institutional base and it is taken as a reference point in the bargaining for the monetary wage. In addition it is reasonable to argue that a level of the market wage systematically higher than the subsistence wage can modify the subsistence wage itself: since it is nonsensical to assume a market wage systematically higher than the subsistence wage the only possible effect of a systematic payment of higher wages than what is required for subsistence is that the standard of living adjusts itself to that imposed by the higher market wage. Veblen implicitly assumes that the subsistence wage is exogenously given and not variable; the comparison is made between the market wage and the subsistence wage when the market wage is lower than the subsistence wage.

2.3 The determinant of economic growth: technology and industrial “sabotage”

In the section 2.2 a reconstruction of the theory of income distribution has been given. Here instead let us see what variables affect economic growth according to the author. Veblen builds a theory of economic growth starting from the distinction between productive and unproductive labour stressing that productive labour produces real well-being, and therefore economic growth while unproductive labor does not contribute to economic growth since it does not produce real income, but just monetary income *via* the mechanism of prices; at the same time however it receives income thanks to the social recognition of the status of unproductive workers. There are several activities that can be excluded from the category of productive activities.

Amongst these, Veblen pays particular attention to financing and business activities on the one hand and to the activity of acquisition and spread of erudite knowledge on the other. It is interesting to notice that unlike erudite knowledge, Veblen attributes a productive effect to technical knowledge since this is materialized in real goods (see Veblen, 2001 [1921], p.19). If technical knowledge contributes to economic growth then workmanship and idle curiosity play a significant role in such a process. So Veblen builds his theory of economic growth mainly relying on the concrete application of good instincts.

Technology is a necessary factor of production and economic growth in Veblen. Let us see why. Veblen regards the *current* production system as an “industrial system”, that is to say as an organization acting within a wide complex system and at the same time as an organization with complex structures inside it. More specifically, the industrial system is a complex organization in which a circular concatenation of interdependent mechanical and communicative sequences supplies conditions of working and of equilibrium. Each element of the industrial system (“section, group or individual unit”) does not act independently from the action of other elements which precede and follow it. Consequently each element of the system - if seen outside the system itself - is not self-sufficient and it is not precisely a “production factor” (Veblen, 1964 [1919a], p.52; see also Veblen, 1904, ch.2). Defining the industrial system in the above terms Veblen emphasises – as O’Hara (1999, p.157) remarks – the *social role of production*. In such terms production is not just a matter of transformation of inputs into outputs. It is something wider. As O’Hara (1999, p.157) writes: in Veblen, “production is fundamentally a social process [...] where the material product [is in] unison in the labor process [...] due to the collective origins of knowledge and the industrial arts”. So the reciprocal dependence of each link in the industrial chain is the necessary condition for the working, survival and “equilibrium of the forces in action”. So this interdependence induces the system to impose a forced process of “co-partnership” of each element with the others (see Veblen, 1964 [1919a], p.87) in processes characterized by regular standardized actions (see Veblen, 1964 [1919a], p.38).

So in the industrial system production follows standardized sequences with features of specialization, impersonalization and mechanization (see Veblen, 2001 [1921], ch.III). Given these characteristics the practical management of the industrial

system is entrusted to technicians who show natural proclivities and attitudes in line with the process described above. While technicians manage the technical aspect of the industrial system, undertakers manage its business plan. In other words the undertakers take over the strategical management of the industrial system. Standardization of processes in fact is functional to the action of undertakers since it brings financial, commercial and mechanical activities into line, assuring greater possibilities of controlling business trends (see Veblen, 1904, ch.3). However the mere reciprocal dependence of the elements within the industrial system is not sufficient for the efficient use of the same. The obligatory mechanism of “co-partnership” assures working, “industrial salvation” and stability but not necessarily ‘efficiency’. In particular the industrial system is ‘efficient’ if it works by “faultless equilibrium”, in other words if: *a*) it produces at its maximum possible level, *b*) it is immune to external interference and *c*) it is “conditioned on a reasonably good coordination of [its] working forces” (Veblen, 1964 [1919a], p.88). In addition Veblen states that:

“Any dislocation, derangement or retardation of the work at any [...] point [...] in this balanced system of work will cause a disproportionately large derangement of the whole” (Veblen, 1964 [1919a], p.88).

With particular reference to points *a* and *c* Veblen stresses that they are technical matters, in other words matters for technicians (see Veblen 1964 [1919a], p.89). Actually he remarks that these points *should be* matters for technicians – the “men skilled in [...] matters of technology” – since it is “reasonable to expect” that control and coordination of mechanical processes are entrusted to people: “experienced in the ways and means of technology and [...] who are in the habit of thinking about these matters” (Veblen, 1964 [1919a], p.89; italics added). Veblen remarks on the necessity for the industrial system to be entrusted to technicians since they have the adequate and disinterested knowledge and skills for its efficient administration, since the efficient administration of industrial capital allows their full utilization, and since the full utilization of capital goods allows the community to reach its potential growth. As Veblen comments:

“The material welfare of the community is bound up with the due working of [...] the industrial system which depends on the expert knowledge, insight, and disinterested judgement with which it is

administered. It should accordingly have seemed expedient to entrust its administration to the industrial [technicians]” (Veblen, 1964 [1919a], p.89).

Thus according to Veblen it is clear that economic growth is a matter of technology – or rather a matter of the best administration of technology – and in Veblen technology is only apparently a matter of capital goods. It is something more. More specifically capital goods, i.e. *materially* productive goods, are a “matter of mechanical efficiency”; mechanical efficiency is then a matter of technology and technology is a matter of the cumulative process of development of knowledge and practice (see Veblen, 1908a, p.517). More specifically, industrial capital is for Veblen “a mechanical application of industry”, so it is first of all the material application of a peculiar kind of habit of thought (Veblen, 1908a, p.526; see also Veblen, 1964 [1919a], p.68) which in turn is a material expression of technological “cultural continuity” between human generations. In fact – as Veblen remarks – capital goods are “an affair of the collectivity” (Veblen, 1922 [1914], p.103). In other words, they are an expression of the evolution of the community’s technological knowledge over time – “industrial art” (see Veblen, 1964 [1911], p.68). Veblen specifically defines the state of “industrial art” in the following terms:

“The state of industrial art is a joint stock of knowledge derived from past experience, and is held and passed on as an indivisible possession of the community at large” (Veblen 2001 [1921], p.19).

We can limit the concept of industrial art to technological knowledge accumulated over time⁶⁶. So the stock of existing industrial capital cannot be intended as the product of *current* technological knowledge since the current technological knowledge in fact adds to something that already exists. Veblen first of all looks at industrial capital in an evolutive and immaterial sense. So industrial capital is an expression of the instinct of workmanship and idle curiosity. These instincts provide the collectivity with a particular manner of viewing the world so current industrial capital can be seen as the material, mechanized stock of accumulated worldviews concerning in particular the use of resources and the serviceability of outputs for tackling the unfriendly and

⁶⁶ Edgell (2001, p.145) – using the Veblenian terminology about tangible and intangible assets – compares industrial art to a social asset both as an intangible asset – expressed by technological knowledge – and then as a tangible asset through the materialization of technological knowledge into technical equipment.

constraining environment. In brief, capital goods are the evidence of the development of instincts and institutions in the direction of matter of fact logic. So development of technological knowledge – materialized into the current industrial capital – is the result of past and current innovation of habits of thought addressed toward the factual interpretation of reality. It is firstly a continuity of “immaterial [and common] assets” and only later of material assets. Consequently industrial capital and its efficiency is first of all a matter of mental habits and proclivities; so technological development and thus economic growth is assured when proclivities are addressed towards a particular kind of reasoning and behaviour. In particular, reasoning must be structured in mental processes of learning, evaluation and judgement in terms of cause-effect, while behaviour must follow precise, standardized processes (see Veblen, 1904, ch.4). In conclusion industrial capital materially shows the evolutive state of the instinct of workmanship, of idle curiosity that is to say the evolutive state of “experience, experimentation, habits, knowledge [and] initiative” (see Veblen, 1908a, p.518; p.521) and it is industrial art on which instincts and institution will continue to advance (see Veblen, 1908a, p.525). Hence, industrial capital has a clearly instinctual origin: the good instincts or, to use other terminology, the group oriented instincts or simply the non-predatory instincts, namely the instinct of workmanship and idle curiosity⁶⁷.

However in the Veblenian vision the development of industrial capital is dissociated from its control. In fact even if the development of industrial capital is the outcome of the development of good instincts, its control is in the hands of undertakers. In fact Veblen points out that the real problem for the collectivity is not the evolution of industrial capitalism but its control. In other words the question is: Who has the right to access the common stock of knowledge involved in industrial capital? And what are the effects of such access? The question is extremely relevant for Veblen because the peculiarity of access to the common stock of knowledge involved in industrial capital is a source of profit and the peculiarity of access is institutional. The *current* institutional mechanism of access to technological knowledge is the right of ownership of industrial capital. So the ownership of capital goods gives the right to take advantage of common knowledge but undertakers possess capital goods for the purpose of gaining private benefits: profits. In Veblen’s vision the

⁶⁷ The connection between technology and social knowledge in Veblen’s thought is also pointed out by Hodgson (2004, p.183) who writes “The individual and the social aspects of knowledge are connected, because the social environment and its ‘common stock’ of experience provide the means and stimulus to individual learning” (see also Lawson, 2006).

ownership of industrial capital is a consequence of the very evolution of knowledge.

As he writes:

“As the common stock of technological knowledge increases in volume, range and efficiency, the material equipment whereby this knowledge of ways and means is put into effect grows greater, more considerable relatively to the capacity of the individual” (Veblen, 1908a, p.524).

In other words, the higher the technological knowledge, the greater the material equipment involved - since “technological development require[s a] large unit of material equipment for the effective pursuit of industry” (Veblen, 1908a, p.524) - and therefore, the smaller the number of individuals that are able to own such equipment. In other words, the greater the number of individuals involved in the production and development of technological knowledge, the smaller the number of individuals that can actually use it. Two important observations derive from this: *a)* technological development is always associated with an extension and growth of material tools; *b)* the enlargement of material equipment is the cause of dissociation between producers of technological knowledge and users. The last point requires a detailed explanation: Interpreting Veblen, it can be argued that the institution of ownership was born as the natural right to own what one has produced. Veblen shows that at low levels of technological development there could be no dissociation between producers and users since the production required a low level of technological knowledge so the individual who produced something naturally became the owner of what s/he had produced. She/he was therefore naturally both producer and user. Then technological development started to characterize production in terms of the co-presence of different knowledge supplied by different individuals. So production was not the outcome of a single type of knowledge but of different ones and consequently it was actually the outcome of different individuals. However, the co-presence of knowledge was not associated with the evolution of co-ownership. Such equilibrium could be guaranteed by the prevalence of good instincts. In fact only the instinct of workmanship combined with the instinct to solidarity could allow ownership to maintain its natural character. Instead the prevalence of the predatory instinct changed the perspective, so the co-presence of knowledge was associated to ownership and not to co-ownership. In other words when someone becomes the owner of what is collectively produced, this individual becomes the only one that has the right to use what it is collectively

produced. Having the right to use technology – and therefore having the right to use industrial capital – is equal to having a market advantage as regards those individuals that are excluded from its use (Veblen, 1908a, p.524). Industrial capital is not only owned under the influence of the predatory instinct, but it is used for business purposes so it is controlled for the purpose of obtaining profits. Following this line, Veblen sees the ownership of capital goods as a source of profit and power:

“To engross [...] the usufruct of the commonplace knowledge of ways and means by taking over such the requisite material as may be relatively scarce and relatively indispensable for procuring a livelihood under the current state of the industrial arts” (Veblen, 1908a, p.525).

As a consequence:

“[The business man] can, of course, not create or initiate methods or aims for industry; [...] but he can decide whether and which of the known processes and industrial arts shall be practiced, and to what extent” (Veblen, 1961 [1901], p.298).

In view of the above, ownership ensures that undertakers can take advantage of social technological knowledge. We need to investigate the way in which undertakers use such “usufruct” to make profits, in other words, it is interesting to look in detail at what Veblen calls the “sabotage” of industrial efficiency, often called “conscientious withdrawal of efficiency” (see Veblen, 1969 [1917], p.755; Veblen, 2001 [1921], ch.1); Veblen, 1967 [1923], p.285), consisting in the reduction of the “net of productive capacity” (Veblen, 1964 [1919a] p.94)⁶⁸. The main tool for increasing profits is the mechanism of prices, in other words, the under utilization of capital which is recognized by Veblen as a manifest tool of sabotage of the concrete possibility of production of collective industrial capital whose effect is unemployment (see ch.1). As he remarks:

⁶⁸ Actually the term sabotage of the industrial efficiency is not a definition created by Veblen. He makes reference to a definition given by The Industrial Workers of the World (I.W.W.) an American trade union with insurrectionary aims (see Veblen, 1932, p.798). The Industrial Workers of the World was established in Chicago in 1905. The main supporters were unskilled workers, low wage workers, emigrants, farm workers, miners and loggers. The I.W.W. sustained the class struggle and the destruction of capitalism. They used strikes and boycotts to achieve their ends, but were opposed to the use of collective bargaining and political action. However the number of IWW supporters was always limited (see De Domenico 1969, p.909) and due to a series of internal conflicts, its life was short. In fact the organization had lapsed by the mid 1920s and only recently (mid 1990s) it has been reorganized. On the history of I. W. W. see Brissenden, 1957; Renshaw, 1967 and Dubofsky, 1969).

“[The] earning-capacity [of capital] is determined by what the traffic will bear, that is to say by curtailing production to such an amount that the output multiplied by the price per unit will yield the largest net aggregate return” (Veblen, 1967 [1923], p.68).

“By historical necessity” (Veblen, 1964 [1919a], p.89) the effective administration of the industrial system is entrusted to undertakers who have institutional tools – *money* – for the effective use of the industrial capital and who are interested in the business side of the industrial system, not its mechanical side⁶⁹. Consequently:

“The conditions of life for the variegated mass are determined by what the traffic will bear, according to the calculations [...] which guide the [upper classes]” (Veblen, 1964 [1919a], p.175).

The predatory action of the undertaker pushes him/her to act merely for a “vested interest” in the industrial system. In other words s/he takes steps to gain:

“By obstructing, retarding or dislocating [the industrial system] at some critical point in such a way as will enable [them] to get the best of the bargain in his dealing with the rest” (Veblen, 1964 [1919a], p.93).

Consequently the action of undertakers affects the working of the industrial system. Actually it could be argued that the industrial system loses its characteristic of a system that grows; this is due to the fact that the circular concatenation of interdependent mechanical sequences always undergoes “interruption[s] and dislocation[s]” which affect its regular working towards potential growth. Its working therefore is often irregular and below the potential growth since each link of the chain of the system is in fact the rival of the preceding and following ones (see Veblen, 1904, ch.3).

⁶⁹ The historical necessities are described thus by Veblen: “as the volume of industry grew larger, employing a larger equipment and larger numbers of workmen, the business concerns necessarily also increased in size and in the volume of transactions, personal supervision of the work by the owners was no longer practicable, and personal contact and personal arrangements between the employer-owner and his workmen tapered off into impersonal wage contracts governed by custom and adjusted to the minimum which the traffic would bear. [...] The employment owner [...] shifted more and more to a footing of accountancy in its relations with the industrial plant and its personnel, and the oversight of the works passed by insensible degrees into the hands of technical experts who stood in a business relation to the concern, as its employees responsible to the concern for working the plant to such a fraction of its productive capacity as the condition of the market warranted for the time being. So the function of [...] the captain of industry, gradually fell apart in a two-fold division of labor, between the business manager and the office work on the one side and the technician and industrial work on the other side. [...] Gradually [...] by this shift and division, the captain of industry developed into a captain of business, and that part of his occupation which had given him title to his name and rank as captain of “industry” passed into alien hands” (Veblen, 1967 [1923], pp.105-106; see also Veblen, 1908b).

In order to investigate this issue in greater depth, let us think of the following question: What is the relationship between ownership and industrial capital? Is ownership indispensable for economic growth? Does the accumulation of industrial capital necessarily require its ownership? Veblen assumes industrial capital as materialisation of immaterial “stock of knowledge and practice” (Veblen, 1908a, p.519). Since industrial capital is a stock of knowledge and since “knowledge [...] is a product of the life of the community” (Veblen, 1908a, p.519) then industrial capital is a product of the community. Consequently industrial capital does not need ownership, whereas on the contrary, ownership needs industrial capital. Ownership is an institution; more specifically, it is a “*dominant and typical* method of engrossing” (Veblen, 1908a, p.527) industrial capital and outcomes of capital goods. Ownership is a “self-regarding” institution based on “personal, invidious, differential, emulative” factors (Veblen, 1922 [1914], p.172). The dominance typical of ownership finds its nature in the prevailing predatory instinct and in its subsequent acceptance as a reputable institution. Ownership needs industrial capital since it supplies its business profits. The owner does not need industrial capital for itself but for its ‘efficiency’ in terms of pecuniary gains. As Veblen remarks “[his/her] business endeavors depend, other things equal, on the efficiency [of the production process]” (Veblen, 1908a, p.538). Actually the owner needs the immaterial knowledge which is behind capital goods. On this point Veblen stresses that ownership assigns (to the owner) - the right to take – in “usufruct [the] industrial art” (Veblen, 1964 [1919a], p.69; see also Veblen, 1967 [1923], p.67). The possession alone of capital goods is not sufficient to obtain profits in business. However the owner should have technical knowledge and training to produce capital goods and to use them. But “[his/her] knowledge and training [...] is of business, not of industry” (Veblen, 1908a, p.536) so s/he needs to *own* external knowledge; in other words s/he needs the service of technicians (see Veblen, 1908a, p.536). As Veblen remarks:

“He [...] needs in his business the service of persons who have a competent working mastery of this immaterial technological equipment, and it is with such persons that his bargains for hire are made” (Veblen, 1908a, p.536).

When the owner owns the service of technicians then capital goods become “means of production”. As Veblen stresses “without them, or in the hands of men who do not

know their use, the goods in question would be simply raw materials” (Veblen, 1908a, p.537). So the service of technicians is functional to the action of undertakers for two main reasons: *a)* undertakers have no technical knowledge of using technology, *b)* undertakers look for efficient technicians since undertakers need more efficient industrial processes not in order to expand real production – which they do not want – but to *save time* in the rotation of capital. On this point Rutherford (1984, p.338; see also Cochran, 1970) interpreting Veblen writes: “under business institutions the problem is that new technology will only be introduced if there is a perceived pecuniary advantage in introducing it”. Hence undertakers positively support continuous technological development only if it is to their advantage. If this does not occur technological innovations are not welcomed and a possible conflict can be generated. Although Veblen does not directly clarify this point, one could argue that conflict is possible when technicians notice that their knowledge does not find concrete application; in fact it is reasonable to think that technicians are not interested in the improvement of knowledge for any intellectual aim but for a concrete materialistic application. Since the goal of ownership is always a predatory aim, Veblen stresses that ownership of the means of production:

“Gives the owner not only the right of use over the community’s immaterial equipment, but also the right of abuse [of community’s industrial efficiency] and of neglect or inhibition” (see Veblen, 1908b, p.106).

So the inhibitory process of undertakers gives rise to the under-utilization of capital goods for the purpose of profits - “capitalisation of inefficiency” (Veblen, 1908b, p.108). More specifically, the inhibitory process entails the utilization of production capacities below the maximum level is the effect of “restraint of trade” followed by the undertaker (see Veblen, 1908b, p.106). With the aim of gaining monetary profits, undertakers limit the production of goods. The limitation of production determines high price levels. Profit is therefore achieved by acting on the price side rather than on the quantity side (see Veblen, 1908b, pp.106-107). So undertakers act directly on quantity control so as to influence prices. In addition since industrial capital is a component of a complex system and since an interdependent part of the industrial system, the effective production capacity of each form of industrial capital affects the productive capacities of the other forms of industrial capital. The under utilization of

some industrial capital is enough to generate under-utilization of the whole industrial system (see Veblen, 1964 [1919a], p.88). In other words sabotage of efficiency is not mainly intended on the microplane but on the macroplane. A micro sabotage determines a macro sabotage that is to say a sabotage of the system (see Veblen, 2001 [1921], ch.I).

However, independently from the way undertakers act on the inhibitory process, the effect of this process is to the detriment of economic growth and employment since production and occupation are generally maintained at a lower level than their potential. In other words, since industrial capital is not used efficiently – to full capacity – the economic system always will work with “ordinary” and “normal” conditions of unemployment (see Veblen, 1964 [1919a], p.97) and with an economic growth rate lower than the potential. As Veblen remarks:

“The recurrence of hard times, unemployment [...] goes to show how effectual is the inhibition of industrial exercised by the ownership of capital under the price system” (Veblen, 1908b, p.108).

So “sabotage” of industrial efficiency is a “natural right of investment”. Since investment is a matter of pecuniary capital and of ownership then “ownership confers a legal right of sabotage” (Veblen, 1967 [1923], pp.65-66). Being the owner of his/her firm the undertaker has an absolute and exclusive use of it. This means that s/he has the right to do what s/he wants with the firm. Restrictions, postponements, and abstentions from the production process represent legitimate choices on the part of owners (see Veblen, 2001 [1921], p.99). Having the right to control the entity of production, undertakers in fact have the right to control employment and economic growth both of industrial equipment and of workers. In the Veblenian logic of profits, the system tends to spontaneously produce low economic growth rates and unemployment since production is maintained at a level that assures a profitable price, so at a lower level than its potential. It could be added that there is an inverse relationship between profits, economic growth and employment⁷⁰. The volume and trend of production are managed according to the market logic. Availability and productivity of inputs and/or social needs are not significant variables for the choices of firms. They are simply functional to firms’ choices. Indirectly it could be argued

⁷⁰ The higher the level of unemployment, the higher the level of profits, and the lower the level of economic growth.

that the sabotage of industrial efficiency is a sabotage of workmanship, that is to say of knowledge and skills. So sabotage concretely reveals itself in the following terms:

“It consists [*a*] in stopping down production to such a volume as will bring the largest net returns in terms of price, and [*b*] in allowing so much of a livelihood to the working force of technicians and workmen, on the other hand, as will induce them to turn out this limited output” (Veblen, 1967 [1923], p.67).

Consequently the right to sabotage – guaranteed by ownership – becomes a convention by which undertakers define and dictate the quantity of goods to produce and distribute. It is canny conduct, or rather “[...] a shrewd balancing of production against price, such as is best served by a *hard head and a cool heart*” (Veblen, 1967 [1923], p.67; italics added). He also writes:

“Profitable sales can be made only if prices are maintained at a *profitable level*, and prices can be maintained only if the volume of *marketable* output is kept within *reasonable* limits [where] reasonable means *what the traffic will bear*, that is to say *what will yield the largest net return*” (Veblen, 1964 [1919a], p.91 italics added; see also Veblen, 1904, ch.3 and ch.5; Veblen, 2001 [1921], p.66).

Veblen in conclusion recognizes technology, the industrial art, as the effective and indispensable factor of growth or rather as an intergenerational and collective factor of economic growth. However, the possibility of the system reaching its potential growth depends on the actual state of ownership of technology and, in view of what has been said above, private ownership appears to be the institution that in fact limits growth.

2.4 Income distribution, economic growth and employment: the role of “wasteful expenditures”

The literature has recently returned to the Veblenian theory of income distribution and economic growth, pointing out how a particular distribution of income can positively or negatively affect economic growth. There are three significant works that can be considered here: a) “*Veblen’s analysis of social wealth, industry-business, and crises of capitalism*” by Phillip Anthony O’Hara (in O’Hara, 2000, ch.4), b) “*Emulation, Inequality, and Work Hours: Was Thorstein Veblen right*” by Samuel Bowles and Yongjin Park (2005), and c) “*Conspicuous consumption and unemployment: a re-reading of Thorstein Veblen’s theory of income distribution*” by Guglielmo Forges Davanzati (2006b). O’Hara argues that a redistribution of income in favour of non-productive sectors reduces the “efficient working of technology” which determines reductions in aggregate production and therefore defining an endogenous condition of limitation of capitalism. On the contrary Bowles and Park show that an unequal distribution of income has a positive effect on economic growth. Forges Davanzati agrees with O’Hara, adding that a redistribution of income in favour of the leisure class increases the demand for luxury goods which determines a reduction of aggregate production and an increase in unemployment. A more detailed description of these three re-interpretative approaches to Veblen’s income distribution and economic growth will be shown below. Let us start with O’Hara’s model.

a) *The contrast of productive-unproductive activities as the limits of capitalism.*

O’Hara’s assumes an economy composed of two main activities, industrial and business activities, and makes use of the ‘corn’ model assuming that “everything is made of corn”⁷¹; he uses the ‘corn’ model for emphasis on material production, as in Veblen. The production of corn is a function of workmanship which – in his view – depends on the existing level of technology, on “worker’s skills and knowledge and on

⁷¹ As he writes: “corn is the material substance of the economy: it is used as food, means of production in the form of seed, plus it forms the building blocks of the motor vehicle industry, [...] fuel, capital goods.[...] Productive workers plant and water the seeds, tend to their growth and development as plants, harvest the corn, transport the corn to market, compress the corn, and use the produce fixed and circulating capital, plus consumer durables and nondurables. Imagine that there are also unproductive workers such as accountants, advertisers, public servants members of parliament, owners of land and capital, banks, and sales workers, all of whom receive corn as payment and deal with numerical data in units of corn. Corn is also used as money: exchange, saving, and credit are undertaken with units of corn as the standard of value. Workers are paid [...] on subsistence wage in the form of credit. [...] Owners of land and means of production, and some of other unproductive agents, save corn in banks”.

the stock and rate of utilization of the available capital stock” (O’Hara, 2000, p.72)⁷². A distribution of corn from industry to business produces a reduction of output and an increase in prices. In this case – he writes – the “additional corn distributed to business is smaller than the net reduction of corn available to industry. A redistribution of corn to business interests [therefore] reflects an increase in wealth ‘*de jure*’ and a decline in wealth ‘*de facto*’, either ‘use-values’, or ‘livelihood’”. More specifically, O’Hara assumes that the industrial sector is able to produce a surplus of corn since the costs of subsistence and replacement of inputs are lower than the contribution to production of the instinct of workmanship. This assumption is in line with Veblen’s thought since:

“Industrial efficiency is presently carried to such a pitch as to afford something appreciably more than a bare livelihood to those engaged in the industrial process” (Veblen, 1975 [1899a], p.25).

The surplus can have several destinations: it can be conserved and given on loan by capitalists to generate new surplus, it can be re-invested in new production, it can be consumed by technicians to expand their knowledge and it can be consumed by workers of unproductive sectors. The issue of distribution of surplus between productive and unproductive sectors is extremely relevant for O’Hara (2000, p.74) since it influences “the degree of stability, regeneration, and expansion of capitalism (in the reproduction process)”. In line with Veblen’s thought, O’Hara stresses that since unproductive sectors do not contribute to the material production of corn, their gains derive from the removal of corn from the productive sector and he adds that the minimum condition for reproduction is that the maximum gains in the unproductive sector are not higher than the surplus itself. This is what O’Hara (2000, pp.82 ff.) calls “the bar of critical maximum exploitation” over which capitalistic reproduction is in fact compromised “and new systems could emerge (for example socialism or fascism)”. In this way, O’Hara (2000, p.76) then tries to define a “rate of business exploitation of industry” expressed as the ratio of “the amount of the surplus [...] utilized for unproductive activities” to “the total product distributed to the productive sector”. Consequently, the higher the costs of the unproductive sectors (interest, wages, etc), the higher the exploitation in industry, and the higher the workmanship – so the higher the proportion of production distributed in favour of technicians, and the

⁷² All such variables are measured in the quantity of corn necessary to their realization.

lower the rate of exploitation in industry⁷³. The corn model proposed by O'Hara shows various limits that the author himself explains in the course of his analysis. As he argues, there are many qualitative factors involved in the production process that cannot naturally have a quantification in terms of corn, so the transformation of everything into corn invalidates the possibility of an exact definition of the "rate of exploitation in industry" and the "bar of critical [...] exploitation". At the same time this does not completely rule out the possibility that a distribution of income in favour of unproductive classes reduces the rate of exploitation instead of increasing it, allowing capitalist reproduction; this is what the author himself calls "the Keynesian element of effective demand" (O'Hara, 2000, ch.4). In this case a distribution of income in favour of the unproductive class can increase the demand for material goods and since unproductive workers are not employed in the productive sectors then the increased demand increases the production and employment of the productive sector. The variation of total product distributed to the productive sector can exceed the reduction of the total product given to the unproductive classes; the consequence is that the "rate of [...] exploitation" is reduced and capitalist reproduction is guaranteed.

b) Emulation and economic growth. Bowles and Park (2005) have shown how *infra group* emulation has a positive effect on the worker's allocation of time between labour and leisure. They build a model making reference to a consumption function for the worker whose components are: *a)* "effective consumption" – defined as difference between worker's income (assumed as the product of wage by working hours) and the average income consumed by the higher reference group, *b)* the hours of work. The choice's variable is the hours of work and the individual maximizes his/her utility function under the constraint of a given wage and consumption of the higher class. Given this function the individual *should* choose the optimum level of working hours, that is to say the working hours that equalize the "marginal rate of substitution between leisure and effective consumption to the wage rate" (Bowles and Park, 2005, p.400). According to the authors the consequence of a distribution of income in favour to the upper class is an increase of income produced by workers; in fact each increase of income for the upper class is consumed by it; an increase in upper class consumption reduces the utility of the single worker and increases the marginal utility of his/her effective consumption as regards the marginal utility of leisure, therefore

⁷³ The reduction of exploitation in industry also occurs if the surplus is accumulated, or given in loans, or re-invested.

pushing the worker to increase his/her hours of work. The authors remark that their model works if two important assumptions are assured: *a)* workers have freedom to choose their hours of work, *b)* workers are engaged “in a conscious optimising process in selecting their working hours” so workers are rational agents; however as they also add, “a more plausible view is that [workers] have norms concerning the appropriate division of their time between family, friends, work, and other activities, and that these norms differ from group to group and evolve over time” (Bowles and Park, 2005, p.401); in their model the supply of working hours must not be limited by institutional or relational constraints; in addition – and as an implicit assumption – no conflictual propensity exists in their mode when income is unequally distributed; in fact if propensity to social conflict is assumed, workers could decide to withhold income from the upper class rather than increase working hours in order to maximize their utility function.

c) waste and unemployment. Forges Davanzati shows that the “Keynesian element of effective demand” in O’Hara does not in fact produce economic growth. The author particularly wants to investigate how the level of aggregate production and employment is negatively affected by an increase in demand for luxury goods *via* an income distribution process in favour of the leisure class. The hypotheses from which the author starts his analysis are: *a)* the economy is divided into two sectors, the luxury goods sector and the wage goods sector; *b)* the macroeconomic system is made up of four social classes, i.e. the leisure class, businessmen, technicians and workers; in particular the leisure class is involved in conspicuous consumption via an income gained in the form of rent; in this case the author regards the rent of the leisure class as the ‘reward’ for profits whose level is equal to a slice of profit where this slice is called “index of the degree of exploitation” of workers. In the model in fact the leisure class is considered a class composed of individuals that do not contribute to the production but that have ownership ‘rights’ on capital since they contribute to the formation of capital – or rather of monetary capital – by “banking and financial intermediation”, which gives them the right to an income. In fact this right is directly established by them through the setting of prices (such as the interest rate). Consequently they remove part of the income produced by workers without contributing to its production, therefore exploiting workers; workers work in the luxury goods sector and in the wage goods sector at a subsistence wage, while businessmen are interested to money profits

and technicians are interested in improving the technical conditions of production so as to expand it. Finally *c*) full employment is assumed. His idea is that an exogenous increase in the income of the leisure class pushes the same class to increase their demand for luxury goods. Thanks to the increase in demand for luxury goods, businessmen increase the demand for labour in that sector. Given the condition of full employment, an increase in the demand for luxury goods moves workers from the wage goods sector to the luxury goods sector. The production of wage goods decreases and firms both in the luxury and in the wage goods sector do not have enough 'basic' goods to pay their workers. In fact since the subsistence wage is fixed, then to maintain the same real level of payment for their own workers businessmen must reduce the number of workers both in luxury and in wage goods sector. The conclusion is that "the higher the rent/wage ratio, the higher the unemployment"⁷⁴.

2.5 The supply and the demand side-effect of rent increases on economic growth and employment

In the above sections a reconstruction and rereading of the economic process of income production and its distribution has been put forward. In addition it has been seen how Veblen builds his theory of income circuit within a schema of credit economy. At the same time he transfers his vision on the traits and working of institutions in the system of income distribution. This allows him to structure a theory of income distribution based on the fundamental assumption that the origin of the economic categories of income – rents, profits and wages – is not economic but institutional. In other words, rents, profits and wages are the outcome of habits of thought and do not have their source in some form of contribution to the production. In addition Veblen seems particularly interested in tracing the foundation of economic growth to technology and its full utilization. Also in this case institutions can slow or quicken the process of growth, labelling ownership as the institution unable to guarantee an effective growth in line with its potential. Ownership structures a habit of thought addressed to the pursuit of monetary profits *via* the mechanism of prices and capitalization, with the aim of expanding firm size and therefore reaching

⁷⁴ On the same lines see also Forges Davanzati (2006c).

monopolistic positions. The result is that ownership leads the system to keep the quantity of production below its potential.

In addition, even though Veblen does not express himself on the effects of a policy of income distribution in favour of undertakers it is interesting to note that the author in fact appears critical of the positive effects of such a policy since the increased profits may not be reinvested. As Veblen writes:

“Business principles, *leading to saving and shrewd investment*, are too ingrained in the habits of modern men to admit an effective *retardation of the rate of saving*” (Veblen, 1904, pp.255-256; italics added).

On the other hand, what can be said as regards an income distribution in favour of the leisure class? In particular does the waste of the leisure class contribute to economic growth or limit it? In view of what has been said above, the waste of the leisure class is a peculiar kind of consumption characterized by its not being strictly serviceable for “community” but just for an institutional motive: envy. In fact in the *Theory of the Leisure Class* Veblen confines his analysis to the nature of ostentatious consumption without investigating its effects. The effects of ostentatious consumption – in particular on economic growth – are instead mainly traceable in the *Theory of Business Enterprise*. The comparison of the effects of waste with its nature is not so simple as might be thought. The reader of the *Theory of the Leisure Class* probably expects a critical reconstruction of the effect of waste on economic growth, so probably thinks that the higher the financial rents, the higher the macroeconomic waste, and so the lower the economic growth. Instead Veblen in the *Theory of Business Enterprise* extols rent as a factor of economic growth. As he remarks: “the wasteful expenditures enhance demand [...] increase profits and raise capitalization” (Veblen, 1904, p.252; italics added). As can be seen, with this quotation Veblen accepts in fact the Malthusian theory of capital accumulation and for this reason such theoretical compatibility can be called the *Malthusian element of Veblen*. There are different quotations that can be taken into consideration to define the Malthusian element. Veblen in fact writes

“The persistent defection of reasonable profits calls for a remedy. The remedy may be sought in [...] an *increased unproductive consumption of goods* [...]. If enough of the work or of the output is turned

to wasteful expenditures, so as to admit of but a relatively slight aggregate saving [...] profitable prices can be maintained on the old basis of capitalization. If the waste is sufficiently large, the current investment in additional industrial equipment will not be sufficient to lower prices appreciably through competition” (Veblen, 1904, pp.255-256; italics added).

First of all waste is intended as a remedy for economic stagnation. In addition if undertakers react to the increase of demand *via* new investments – in particular reinvesting the accumulated profits – then their possibility of new profits increases since they enlarge their control of the market, maintaining prices at a high level as regards a more competitive system. Moreover, the higher the waste, the higher the expectation of profit, so the higher the tendency to make new investments.

So, from the above quotations it can be argued that Veblen has an idea of economic growth led by the demand side and by a distribution of income in favour of the leisure class, who show the highest propensity to consumption. Such an idea is extremely close to the relationship between unproductive consumption and economic growth in Thomas Malthus’s *Principles of Political Economy* (1820)⁷⁵. Malthus points out the positive effect that an increase in unproductive consumption has on capital accumulation. In fact given a level of productive workers, and therefore given a level of production, an increase in the income of the unproductive classes determines an increase in demand which firstly absorbs the same production, then makes prices and profits rise, thus pushing firms to increase their investments⁷⁶. More specifically, Malthus stresses that production may reach levels that may not be absorbed by workers and capitalists because of the capitalists’ excessive tendency to savings and investments and due to the fact that workers cannot consume more than what they receive in wages. Output that is not absorbed by workers and capitalists can lead the market to a situation of overproduction and Malthus finds the solution to this problem in the unproductive consumption of landlords. Veblen directly expresses the acceptance of Malthusian theory of growth in the following way:

⁷⁵ It might be useful to recall here that classical economics makes reference to productive consumption to identify the consumption of workers employed in the material goods production sector while with the term ‘unproductive consumption’ classical economists identify the consumption of individuals not directly employed in the sector of production of material goods.

⁷⁶ On the Malthusian theory of income distribution and economic growth see, amongst others, Eltis (1980); Costabile (1980; 1983), Costabile and Rowthorn (1985).

“It will be seen that on this view of the effect of wasteful expenditure the position occupied by [...] Malthus [...] is substantially well taken, although the defence of waste which [this economist offers] may be incomplete. Waste seems necessary to keep trade brisk, and therefore to keep the industrial processes working at their full capacity. The ulterior reason for this state of the case being the fact that the decisive ground which determines the margin of activity in business, and therefore in industry, is the business men's reluctance to accept a reduction of profits as measured in terms of price. The opponents of the Malthusian view failed to appreciate the decisive importance of price, as contrasted with serviceability, among the motives on which business proceeds” (Veblen, 1904, p.253, footnote 37).

From the above quotations it can be said that the tendency to under-utilize capital perpetuated by undertakers can be neutralized by an increase of leisure class rent and at the same time undertakers do not suffer a fall in prices – “the decisive [...] motives on which business proceeds” – if the leisure class keeps its demand high.

The Malthusian element of Veblen can be expanded in the following terms. Let us assume an initial condition where unemployment exists. The increase in rents produces an increase in the demand for luxury goods which produces an increase of investment in this sector. The effect is growth and employment in the luxury goods sector; in addition since the number of workers is increased in the luxury goods sector, the demand for wage goods also increases, so undertakers increase investment and employment also in the wage goods sector. Thus the increase of rent has produced an increase in global demand *via* the increase in consumption which then pushes undertakers to increase investments and so to increase production and employment in the system. The same result occurs if the Veblen effect is in operation. In fact when rent increases, the leisure class increases its consumption. Given an increase in demand for luxury goods, undertakers raise prices. If prices of luxury goods go up, members of the leisure class increase their demand for them. Production becomes profitable since undertakers increase investments and demand for labour in the luxury goods sector increases. Given an increase of employment in the luxury goods sector, the demand for wage goods increases and undertakers increase investments and employment also in the wage goods sectors. In conclusion the effect of an increase of rent combined with the Veblen effect is: increased employment, production and profits in the system. Note that the Malthusian element of Veblen cannot be intended as the “Keynesian element” mentioned by (O’Hara, 2000, ch.4) for at least two reasons: *a*)

the positive effect of rents is not driven by public interventions aimed at the increase of employment, *b*) the multiplier effect is absent in Veblen.

However at the same time it has been seen that financial rent is a cost – a “charge” on profits – for firms which can reduce investments, so it can slow economic growth. Veblen remarks for example that the interest rate “diminishes the aggregate net profits [...] in that it requires them to pay interest” (Veblen, 1904, p.112). His critical position about financial rent on economic growth is then particularly clear in his *The Vested Interests and the Common Man*. Here in fact the author writes:

“Productive industry yields a margin of net product over cost [...]. This margin of net product has come to rest upon productive industry as an overhead *charge payable to anonymous outsiders who own the corporation securities*” (Veblen, 1964 [1919a], p.48; italics added).

The following quotation appears clearer:

“Rent is [...] a case of charging what the traffic will bear; and rental values should properly be classed with these intangible assets [...] which are due to their effectual control of the rate and volume of production” (Veblen, 1964 [1919a], p.74).

In comparing the Malthusian element of Veblen with his approach on rent as a financing cost, a problem of internal consistency might be noted in Veblen’s thinking. In fact the parallel reading of the Malthusian element with rent as a financial cost can lead towards this conclusion. However, a different perspective can be gained if the reading of the two effects is seen in sequential terms from the Malthusian element to that of rent as a financial cost. The key is in the following quotation: “Waste seems necessary to keep trade brisk, and therefore to keep the industrial processes working at their *full capacity*” (Veblen, 1904, p.253, footnote 37; italics added). In other words the positive effect of the Malthusian element on economic growth is continuous as long as capital is fully used, so until full employment is reached. Expanding Veblen’s thought on the topic, it is possible to continue in the following terms: further increases in rents reduce production and employment. Let us see why: an increase in rent determines an increase in financing costs both in the luxury and in the wage goods sectors; increased rent means increased demand but since there is a condition of full employment undertakers cannot increase investments and production. Rent therefore prevails as a cost in the sense that financing costs reduce profits; if profits decrease,

investments decrease too and the effect of a reduction of investment is a reduction of production and unemployment. In addition since financing costs are rising, firms raise prices both in the luxury and wage goods sectors. In the luxury goods sector the influence of the Veblen effect again pushes the leisure class to increase rent via the increase in interest or buying stocks and bonds; this again determines a reduction of profits, investments, production and employment. On the other hand, the increase in prices and the reduction of investments reduces the workers' real wages; the direct increase in prices reduces real wages while if investments decrease, real wages decrease since total output decreases and prices increase. A cut in the real wage has a negative effect on the level of expected demand which leads to a drop in investment, production and employment. As a result, when the full employment condition is assured, rent stops economic growth and increases unemployment.

Chapter III

DISTRIBUTIVE DYNAMICS AND INSTITUTIONAL CHANGE

3.1 The evolutionary analysis of institutional change

Edgell (2001, p.76) has argued that the Veblenian theory of evolutionary change is “a neglected aspect of his corpus” but “central to an understanding of the coherence of his overall contribution” (see also Edgell, 1975). Edgell (1975, p.76) remarks that the lack of interest about Veblen’s theory of evolutionary change has a well defined historical contextualization: evolutionary theories in general were particularly in vogue in the nineteenth century and the theoretical debate in the following century naturally lost interest in them in apart from the debate in a sector of economics (see for example Hodgson, 1994) and in sociology (see for example Sanderson, 1994). In accordance with Edgell’s view of the centrality of Veblen’s theory of institutional evolution to his thought, the aim of this chapter is to investigate the institutional change – which is substantially a change in the habits of thought – in the specific form of a change driven by income distribution in the Veblenian perspective. This is not a direct line followed by the author in the explanation of the institutional change. He in fact directly followed other pathways mainly based on the role of technology and technicians. Before structuring a Veblenian theory of institutional change *via* distribution dynamics it is useful to look at the author’s vision of the evolutions of institutions until his time and his vision on the perspective for new changes.

With particular reference to his evolutionary analysis of past institutions, Veblen uses a methodology based on historical study⁷⁷ and mainly makes reference to four eras, each of them characterized by different environmental conditions, by peculiar instincts and by a different technological development. These eras were: *a*) primitive savagery, *b*) the barbaric era, *c*) the period of the handcraft economic system, and *d*) the ‘current’ time of mechanical technology (see Anderson, 1933; Bowman,

⁷⁷ Veblen defines history – in particular the history of economic life – in the following terms: “[it] is a cumulative process of adaptation of means to ends that cumulatively change as the process goes on, both the agent and his environment being at any point the outcome of the last process” (Veblen, 1961 [1898c], p.74).

1973, p.xvi; Edgell, 1975; 2001, p.77; Uselding, 1980; Jamison, 1989). Geographically they mainly cover Northwestern Europe and – but some of them – North America. Veblen describes these eras in terms of cyclical movements of instincts and institutions combined with cyclical movements of conflicts and peaceable periods. In Veblen's analysis the reasons such eras alternate seems to be outside the scope of his inquiry, and nor is it clear why conflicts alternate with peaceable periods and *vice versa* or why such conditions are external rather than endogenously determined. Consequently some matters remain open, such as whether conflicts and peaceable periods are driven by instincts and institutions or *vice versa*. In addition he often regards technological changes as the main variable of institutional changes, however, if we assume that technology is an instinctual and institutional matter itself – originating from the instinct of workmanship and institution of industry – then institutional change is in fact the outcome of institutions. This point is well explained by Banks (1959, pp.234-235) who remarks that “since workmanship is to be conceived of as the product of interaction between normative and conditional elements in economic behaviour, changes in the purely technological side [...] will result in change in the norms governing workmanship practices”. In brief, in the evolutionary analysis of institutional change Veblen is not clear in the structure of the cause-effect relations between the socio-economic variables entailed in the changes. Given the above premises let us now see these eras in more detail:

a) *The peaceable era*. Temporally, Veblen places the peaceable era between an undefined beginning and the Neolithic period. Geographically it involved only Northwestern Europe and was characterized by small social communities, agricultural activity, shared inputs and absence of ownership. As Anderson (1933, p.606) writes “[people] entered the [Veblenian peaceable era] with only the most meager stock of knowledge and the crudest of economic technique, but emerged at its end with an imposing body of technology applied with marked success”. Moreover, as Edgell (1975, p.273) adds: “during the [Veblenian] peaceable era [...] the low level of technology preclude[d] a surplus [...] and ensure[d] that workmanship, upon which the survival of the group depend[ed], prevail[ed] as the major force shaping the cultural life of that period”. More specifically in this era people improved agriculture and breeding techniques and started to manufacture objects both for use and for decorative purposes. On the instinctual plane, this period saw the prevalence of the following

instincts: the parental bent, idle curiosity and workmanship and on the environmental plane, people lived in a peaceful state.

b) *The barbarian era.* This era characterized the process of development of Europe between the end of the Neolithic and the Middle Ages. The environment context in which people lived was one of war and the production of surplus (see also Edgell, 1975, p.274). Such a context – as it is summed up by Anderson (1933, p.607) - “gave rise to a general attitude of belligerence” and to the appropriation of things by aggression. As a result, people developed the predatory instinct and the mental attitude to ownership which in turn spread the concept of “status” and therefore the concept of social superiority and inferiority. The predatory instinct changed the method of acquiring things: from production and exchange to simple aggression. A change in this direction makes the need for “useful effort” irrelevant – and as Anderson (1933, p.610) says - there was no “stimulus to technological progress”.

c) *The handcraft era.* Veblen recognized the handcraft era as a relatively peaceable era. Geographically it involved both Northwestern Europe and North America but for different time periods. More specifically, it covered the period between the end of the Middle Ages and the beginning of the eighteenth century in Europe and the early nineteenth century in North America. On the instinctual plane the predatory instinct and the instinct of workmanship moved in parallel. In particular the era can be divided into two phases of development. First of all, and unlike the previous eras, the system of production moved from an atomistic system to a corporative one with limited exchanges. The second phase featured a marked development of large scale industrial technology and of the means of transport and communication. Correspondingly the scale of production and exchange increased and the single production unit gave way to industry and to international trade. The enlargement of production units and the expansion of trade changed the ‘physiognomy’ of the market in the sense that market relationships started to become impersonal. In addition, in such a phase, ownership spread further to involve in a strict sense the ownership of firms which started to change their nature and goal: from investment for real profit to investment for monetary profit (see Anderson, 1933, pp.610 and ff.) As Edgell (1975, p.275) writes, in this phase “work in order to gain a livelihood is transformed into work in order to gain a profit”. In addition it gave rise to the first wage work. The possibility of directly owning industrial techniques was limited to a small part of the

community, so the majority of the community could only exchange its own activity for an income. It was therefore the era of the beginning of the current social divisions: capitalists on one side and workers on the other. However the activity of workmen was mainly that of using mechanical tools.

d) *The machine era.* New wars and a new technological revolution characterized the environmental context of the machine era. Industry organized itself in a system and workmanship was subjected to the predatory instinct. Impersonal relationships became the market rule and using the words of Arrow (1975, p.6) “the impersonal relationships characteristic of the modern [Veblenian] market[...] impl[y] much more possibility for irresponsibility on the part of sellers”. Consequently there were in fact no checks to inhibit undertakers’ predatory instinct. In addition workers lost their active role in the production becoming “assistants”. As Anderson (1933, p.613) writes “rather than [...] user[s] of machines, [they are] used by them” and Edgell (1975, p.276) adds that the “worker ceases to be an individual, creative productive agent and becomes a machine attendant”. Moreover, “in contrast to the handcraft era in which the owner-worker surveyed and regulated the productive process personally, in the machine era the financial aspects of production become [more important] for businessmen” (Edgell, 1975, p.276).

From this evolutionary analysis of institutional change Griffin and Karayiannis (2002) point out that Veblen identifies two kinds of capitalism: a) a *pro* development capitalism and b) an *anti* development capitalism. In the first case the entrepreneur is at the same time owner, manager and innovator while in the second case the entrepreneur is just the owner. *Pro* or *anti* development is the effect of the different nature of profits and role of innovations. The owner being simultaneously also manager and innovator means that profit has the nature of income of labour income and innovations serve to increase profits, while if the capitalist is just the owner then profit simply becomes capital income, pure investment return. Here innovations are not strictly needed – think for instance of intangible assets – or if needed they are not large enough: think for instance of the related need for undertakers to reduce the rotation of capital and at the same time to under-use it (see chapter 2).

3.2 The Veblenian perspective of future institutional change: the role of technicians

The secondary preliminary part of Veblen's thought that requires particular attention – before looking at the relationship between the distributive dynamic and the institutional dynamic – is his vision of the role of technology and technicians in new institutional changes. As seen in the preceding chapters social well-being is a complex matter for Veblen; it in fact depends on institutional-economic and ethical matters such as *a*) development of technological knowledge and *b*) elimination of waste. In particular in Veblen's thought the elimination of waste is driven by the development of technological knowledge. Technology therefore appears to be the fundamental social variable that can change habits of thought in favour of the collectivity since it spreads the habits oriented to efficiency. As the author remarks the well-being of the community is an industrial matter: it “depends on the state of industrial arts” he writes (1964 [1919a], p.55). Well-being therefore concretely depends on the “maximum production of which the community is capable” (Veblen, 1964 [1919a], p.55); however the maximum production is a necessary condition for Veblen for the improvement of the well-being of the collectivity but it also needs a particular use, control and management which are institutional factors. Since each economic development is always a matter of habits and of changes in habits (see Veblen, 1961 [1898c], p.75), the potential and actual material well-being is always a consequence of the effective state of institutions (see Veblen, 2001 [1921], ch.V)⁷⁸. So social well-being on the part of workers is *an outcome of an institutional trade-off*; and as a result the prevalence of the institution of ownership leads society towards a particular well-being – in favour of the “upper classes”- while the prevalence of the institution of industry leads towards another – in favour of the “inferior classes”. In Veblen's view, the institution of ownership does not favour social well-being for workers; it just assures well-being for a small part of society and the *current* institution – ownership – is a concrete obstacle to the well-being of society as a whole. In order to guarantee social well-being there must be an institutional change, or rather Veblen thinks of institutional changes that lead to the elimination of the institution of ownership and to

⁷⁸ The control of the sector of transport of resources, goods, services and people is objectively one of first strategic elements for an increase in well-being according to Veblen. More in general, social mobility and mobility of resources represent the first step for a process of changing the existing situation (see Veblen, 2001 [1921], ch.VI).

the setting up of a new order in which capital is managed in favour of the collectivity and not for single social classes. So in Veblen's vision such a new social order is implemented by institutional changes the basis of which lie in technological change. As Rutherford (1984, p.126) argues – in Veblen's vision – “new technology significantly affects the conditions of livelihood for some portion of the population in such a way as to induce new habits of thought and action which run counter to the existing institutional norms and vested interest”. According to Bush (1987, p.1087) Veblen's sense of technology must be understood in a broad sense, not only as a strictly technical and mechanical matter. As the author stresses when Veblen speaks about technological change he is not referring simply to mechanical innovations. In his vision the term ‘technological’ is used in a technical-institutional sense; in other words technological change is first of all a change that affects “the problem solving processes” which then is reflected in “a given state of the arts and sciences” and not *vice versa*. Consequently a mechanical innovation cannot exist if *a priori innovation* of “the problem solving process” does not occur. On this point Bush (1987, p.1087) writes “the problem-solving processes of the community generate innovations in the ways of bringing material things to account, thereby changing the industrial environment in which the community works and this changed environment produces further changes in prevalent habits of thought about how to conduct the community's affairs”. In other words, Veblenian institutional change is driven by technological change following a precise logical chain: institutional changes lead to technical changes which in turn lead to new institutional changes; in particular the first step of institutional change is connected to changes in “problem solving processes” and it is a matter of a small part of society, identified by Veblen as the technicians; then new technology produced by technicians – an expression of an institutional change – changes institutions again but differently from the first step, in this last step the whole collectivity is affected by the change. The basis of institutional change is the change in the “problem solving process”; in fact this change has an instinctual source, being a consequence of the instinct of workmanship and idle curiosity, and since Veblen attributes these instincts to technicians, then institutional change is driven by technicians.

Technicians technically manage the regular working of the industrial system. The regular working of the industrial system does not mean necessarily efficient working.

Efficient working means full utilization of capital which is not a matter for undertakers. In addition, the peril of micro sabotage is its spread into the whole system (see Veblen, 2001 [1921], ch.III) which means sabotage of collective knowledge. Consequently through sabotage undertakers control technicians' knowledge and skills; if undertakers – in business matters – use the industrial capital at a level below its full capability then they in fact use knowledge at a level below its potential, the effect of which is reduction of growth potential and unemployment. Consequently, according to Veblen, the strategic control of a single component of the system - given to undertakers - determines strong perturbations of the same; on the other hand, the well-being of society is connected to the regular and efficient working of the industrial system which depends on technicians' realistic possibility of managing the single components of the system itself. So Veblen thinks that a society's possibility of development – in terms of collective well-being – depends on technicians conscientiously taking over the industrial system following the recognition of their social role. The role of technicians is not only addressed to the best technical management of the industrial system but also to institutional change thanks to the spread of habits oriented to efficiency; the strategic and operative working of the industrial system in such a direction should be concretely managed by a complex organization of technicians provided they act as technicians of production and not as speculators. In this sense Veblen argues that unfortunately his perspective of institutional change is not simple since technicians are not immune from business habits of thought: the closeness of technicians to undertakers and the achievement of large gains for their activity concretely reduces the possibility that technicians will voluntarily change the state of things. So an additional condition of institutional inertia can be generated by the behaviour of the technicians themselves rather than the leisure class. A concrete negative example of such an additional condition of institutional inertia is described by Veblen in reference to the actual management of "Federation of Organized Trade and Labor Unions", a union of technicians created in 1881 in Pittsburgh⁷⁹. Describing, among other things, the management of this union (see also

⁷⁹ It is important to notice that Veblen does not directly deal with the Federation of Organized Trade and Labor Unions; he discusses the American Federation of Labor (A.F.L.). However in the Italian edition of Veblen's *Engineers and the Price System* edited by Francesco De Domenico (1969, p.961, footnote 1) the author clarifies that the A.F.L. was in fact the same organization which was born using the name of Federation of Organized Trade and Labor Unions but then changed its name to the American Federation of Labor.

Walker, 1977, pp.231-232) Veblen remarks that society lost an opportunity for change since the Federation was characterized by speculative conduct towards undertakers. Its leadership was entrusted to bargaining technicians rather than to production technicians. The organization in fact was a business organization dominated by a predatory instinct against undertakers, so its actions were mainly aimed at obtaining high gains by defeating employers. It acted exactly like the undertakers since its main object was to sell its products at a high price: In other words this organization acted precisely to keep technicians' wages high in the same way as undertakers act to keep the prices of their products high. The consequent favouritism of its members went against the interests of the community (see Veblen, 2001 [1921], ch.IV). The negative experience of the social role of such organizations makes Veblen lay down possible lines of conduct for technicians for the correct changing of the institutional order. In chapter VI of his *The Engineers And the Price System*, the author draws up what he calls "a memorandum on a practicable soviet of technicians". In Veblenian thought the point of departure of an efficient use of resources is the control of processes of production and distribution of goods and services. For this purpose it is necessary to set up a national or "central directorate" of technicians – helped by "sub centers and local councils" (Veblen, 2001 [1921], p.89); such a "directorate" would be composed of "several thousand technically trained men scattered over the face of the country, in one industry and another" (Veblen, 2001 [1921], p.86). In particular the "directorate" takes the form of a "tripartite executive council" composed of three groups of engineers with different skills: a) "Resource Engineers" with competences on raw materials, b) "Production Engineers" with competences on mechanical equipment and industrial processes, and b) the group of engineers with competences on the "transportation system" and the "distributive traffic in finished products and services" (see Veblen 2001 [1921], pp.89-90). The activity of this "directorate" is made up of several tasks; first of all it must implement the preliminary "cadastration of the country's industrial forces" and then a precise classification of the existing industrial system based on type and size of "energy, resources, materials, and manpower" (Veblen 2001 [1921], p.86). Given such information the "directorate" must then order the system on the basis of three particular activities: "productive industry, transportation, and distributive traffic" (Veblen, 2001 [1921], p.89). On the basis of such preliminary operations the "directorate" is involved then in drawing up a plan of

efficient “administration of industry” at least of “greater primary industries” and of the “country’s transportation system” (Veblen, 2001 [1921], p.88) which must establish:

“the due allocation of resources and a consequent full and reasonable proportioned employment of available equipment and man power; [b] the avoidance of waste and duplication of work”; [and c] an equitable and sufficient supply of goods and services to consumers” (Veblen 2001 [1921], p.88).

In the above policy of change, the role of economists – named “consulting economists” – is not neglected by Veblen. As he remarks “it is also evident that in its continued work of planning and advisement the directorate will require the services of an appreciable number of consulting economists” (Veblen, 2001 [1921], pp.89-90). Finally Veblen gives some indications on the modalities of the take-over by technicians. In particular the technicians’ take-over is a result of social conflict brought about by technicians via general strikes but after the realisation of two preliminary conditions:

“(a) An extensive campaign of inquiry and publicity, such as will bring the underlying population to a reasonable understanding of what it is all about; and (b) the working-out of a common understanding and a solidarity of sentiment between the technicians and the working force engaged in transportation and in the greater underlying industries of the system” (Veblen, 2001 [1921], p.103).

The Veblenian “memorandum” places emphasis on the role of technicians in institutional change, or the “revolutionary overturn” as it was called by Veblen (2001 [1921], p.96). However, technicians realistically remain a *potentially revolutionary* class (see Layton, 1962; 1971; Maier, 1970) and not an effectively revolutionary class; in other words technicians have the basic instinctual and institutional qualifications needed for the change, but the potentiality does not find concrete form because of their concomitant closeness to business culture. This point is also remarked by Layton (1962, pp.70-71) who suggests that technicians just remain a potentially revolutionary class; in his vision Veblen attributes an excessive revolutionary capacity to technicians; Layton criticizes Veblen because he was too confident that the evolutive state of the instinct of workmanship and the historical state of “conditioning of the machine process” were at an ideal level for a revolutionary action. On the contrary, in Layton the facts thwarted Veblen’s positive vision since technicians in practice

maintained a concomitant radical-conservative position in the sense that they did not completely reject the business culture, implying that the “conditioning of the machine was not complete”. Walker (1977, p.229) adds “[technicians] are motivated by a desire for monetary gain, which leads them to pursue pecuniary principles of efficiency [..]. Businessmen are still in authority, but their inability to exercise their responsibility competently prevents the attainment of efficiency. This does not offend the technicians. Their pecuniary motivations lead them to cooperate willingly with the businessmen in limiting the productiveness of the industrial system”. The concomitance of radical and conservative traits in technicians are actually present in Veblen himself; in fact when he critiques the activity of the “Federation of Organized Trade and Labor Unions” he is expressing perplexities on the effective possibilities of creating a revolutionary class of technicians.

Interpreting Veblen’s thought on the revolutionary role of technicians, Edgell (2001, p.139) remarks that actually the main problem is not to look at technicians’ real capacity to be a revolutionary class but to answer the following question: Was Veblen really pervaded by an ideal of a “society of engineers” (Edgell, 2001, p.139) or by the “engineering of society”? (Layton, 1962, pp.70-71). Edgell (2001, p.145) interprets the Veblenian view of technicians’ role in a different way. In his interpretation Veblen sees technicians as “the best-qualified group to *initiate* and *direct* the [necessarily institutional] change” rather than as the social class designated to a direct control of society: in brief, technicians as masters of change rather than rulers of society. As Edgell (2001, p.145) writes, “Veblen consistently argued that what was the best interest of the community, was that production should be managed by those technically qualified”. So technicians must be seen as masters of “technological knowledge” and their positive role in the society is only that of spreading such knowledge and not directing society. Veblen apparently seems to think about a “society of engineers” but this interpretation is only true if the reading of Veblen is limited to the *Engineers and the Price System*⁸⁰. A wider reading of Veblen’s writings leads to another interpretation. In fact as Bell (1963, p.27) remarks, *Engineers and the Prices System* “can [just] serve as a simplified introduction to his ideas”, so interpreting the whole of his thought it is possible to say that Veblen is more interested in the “engineering of society”, in other words in the spread of the instinct of

⁸⁰ Cf. Tilman (1972, 1973, 1988, 1992, 1996) and Stabile (1984, 1986, 1987, 1988) on the debate about the consistency/inconsistency of *Engineers and the Price System* with other writings by Veblen.

workmanship rather than in a “society of engineers”. The ways such a spread can occur are not clear in Veblen since the main social class delegated by the potentiality of action – technicians – is not concretely able to act.

Finally some authors (see for example Bell, 1963; Layton, 1962, 1972; Dorfman, 1973; Hodgson, 1999; Edgell, 2001) argue that the debate about the theory of institutional change in terms of society of engineers or engineering of society is in fact a debate about Veblen’s utopia. His theory of institutional change managed by technicians is in fact unrealistic and therefore utopian. Bell (1963, pp.33-34) for example calls Veblen a “technocratic utopian”⁸¹. Edgell (2001, p.154) adds: “Veblen’s analysis of engineers in EPS and elsewhere is clearly utopian, since it involves a withering critique of the existing price system”. In addition he writes “[Veblen] developed [his utopia] by conveying the idea of a better society, one that gave free reign to the instinct of workmanship, and by speculating on the problem of agency”⁸².

3.3 Income distribution and institutional change: the “limit of tolerance”

In the preceding section the description of Veblen’s theory of institutional change has been presented. It has been pointed out that Veblen traces the lines of development of institutions for the past, he describes the current condition and then he traces the lines for possible new changes making reference to technology as the driving force of this change and to technicians as the social class primarily involved. The aim of the following section is to present a different perspective of change in which the dynamic of income distribution plays an important role and in which the social groups directly involved are workers and the leisure class. The investigation into the dynamics of income distribution and institutional dynamics calls for some important premises elaborated by Veblen. According to the author any institution is *cause* and *effect* of ‘natural’ selection and the process of selection follows the criterion of efficiency. Interpreting Veblen it is possible to say that an institution is efficient if it allows the “enhanc[ing of] human life on the whole” (Veblen, 1975 [1899a], p.99). Pragmatically

⁸¹ For a reconstruction of the debate on utopia in Veblen see Edgell (2001, pp.151-156).

⁸² Edgell (1975, p.268) also argues that the utopian influences in Veblen are due to the contribution of the utopian reformer Edward Bellamy (1951 [1888]).

the enhancing of human life is a matter of material well-being in Veblen. In the Veblenian vision an institution is subject to reform when the well-being of some social classes produced by the use of the institution itself is obtained to the systematic and intolerable detriment of the well-being of some other classes.

In addition Veblen elaborates a logic of institutional change according to which institutions at time t are the effect of selection of institutions at time t_0 and the cause of selection of institutions at time t_1 since they are “[..] the result of selective and adaptive process [and] efficient factors of selection” (Veblen, 1975 [1899a], p.188). On this point Bowman (1973, p. xvii) remarks that “social change or evolution according to Veblen [is] a product of a complex process in which human thought and behaviour – by adapting to a changing social environment – [transforms] the institutional basis for later selection”.

Life in an unfriendly environment in fact requires both an individual adaptation to given circumstances and a change of the circumstances themselves; the concomitant hypothesis of institutions as cause-effect of natural selection finds its grounds in the idea that natural selection - to which Veblen makes reference - has a social rather than natural nature. The environmental circumstances are social, and being social they are institutional circumstances; consequently adaptation and development is a social process not a natural or biological one. As Veblen remarks, institutional change is a process of selective adaptation of habits of thought under the stress of *the circumstances of associated life* (Veblen, 1975 [1899a], p.213; italics added). In this way, the hostility of the environment is a human hostility: it is the outcome of human action and interrelation. More briefly, environmental hostility is a hostility of institutions and it results from the diffusion of particular institutions rather than others. On this point Veblen writes:

“For the purpose of my inquiry – an inquiry as to why and how the habits of life and thought of the individual come to be modified – for this purpose customs, conventions, and methods of industry are no less effective elements in the environment than climate and topography, and these vary incontinently” (Veblen, 1899b, p.111).

On institutional change the following quotation is particularly interesting:

“The growth and mutations of the institutional fabric are an outcome of the conduct of the individual members of the group, since it is out of the experience of the individuals, through the habituation of individuals, that institutions arise; and it is in the same experience that these institutions act to direct and define the aims and end of conduct” (Veblen, 1961 [1909a], p.243).

From the above quotation it is possible to structure a logic of the concatenation of events within the process of institutional change: *a)* institutional change is first of all an outcome of conduct when the same is not supported by any experience; *b)* institutional change forms a new institution when the initial conduct without experience becomes routine conduct and therefore when it is supported by experience; *c)* finally the institution formed by the conduct manages the conduct that has formed the same institution. Following Jennings and Waller (1994, p.1002) in this way Veblen builds a theory of institutional change in terms of “*endogenous* cumulative causation”; consequently a new institution will be born from the previous one and its *hereditary characters* – “usages, customs, conventions [and] preconceptions” (Veblen, 1922 [1914], p.39; italics added) - (Veblen, 1922 [1914], p.38-39) are transferred by “the discipline of habituation” in terms of “tradition, training [and] education” (Veblen, 1922 [1914], p.38-39) to subsequent new institutions. In addition Veblen remarks:

“Institutions are products of the past process, are adapted to past circumstances, and are therefore never in full accord with the requirements of the present” (Veblen, 1975 [1899a], p.191).

From the above quotation it can be seen that social well-being is always historically contextualized. Its historical contextualization does not naturally supply complete efficiency to institutions since they have adapted to a different and outdated sense of well-being. Then Veblen adds:

“[...] The law of natural selection, as applied to human institutions, gives the axiom: “*Whatever is, is wrong*”. Not that the institutions of to-day are wholly wrong for the purposes of the life of to-day, but they are, always and in the nature of things, wrong to some extent. They are the result of a more or less inadequate adjustment of the methods of living to a situation which prevailed at some point in the past development; and they are therefore wrong by something more than the interval which separates the present situation from that of the past” (Veblen, 1975 [1899a], p.207; italics added).

Veblen does not deny efficiency to past institutions – the cumulative process of development of institutions in fact would not allow it – but such efficiency is not enough for current conditions; so when he says that “whatever is, is wrong” he means that the current institutions are efficient to some extent just as they are wrong to some other extent. An important consequence is the identification of the individuals that judge the extent of what is right or wrong in an institution as regards the current necessities. Veblen attributes such judgement to technicians who, however, are not completely able to act ‘rightly’, so an alternative could be proposed, i.e. the evaluation of the extent of what is right is up to the common man at least due to the simple fact that s/he – as the first level of the social hierarchy – immediately perceives possible perturbations of the state of well-being as regards the other chains of social hierarchy. As Veblen remarks:

“The underlying population is dependent on the working of [the] industrial system for its livelihood; and their material interest therefore centers in the output and distribution of consumable goods, not in an increasing volume of earnings for the absentee owners. Hence there is a division of interest between the business community, who do business for the absentee owners, and the underlying population, who work for a living” (Veblen, 2001 [1921], p.67).

Cummings (1899, pp.437-438) critiques Veblen’s sense of “whatever is, is wrong” stressing that it might be better to say “whatever is, is imperfect”. Coherently with his critique of Veblen’s theory of institutional inertia (see chapter 1) Cummings remarks that whatever is, is not wrong, it is just imperfect because if it were wrong than all cumulative process of development would be wrong too. So what is now is right as regards what has been until now but it is wrong – or rather it is imperfect – as regards what will be from now onwards. The imperfection of current institutions is connected to the imperfection of knowledge and experience as regards current conditions; in other words in Cummings knowledge and experience are aimed at improving the present condition not at destroying it. So the existing protected institutions at a given time are the best result of what the society has known from the beginning of evolution until now, but they are imperfect as regards what the same society will know from now onwards.

Given the above premises now let see more specifically the matter of dynamics of income distribution and institutional dynamics. As it has been said, the social

classes involved in such a process are the leisure class and working class and on this Veblen differs; in fact in the previous sections it has been shown that institutional change originates in technological change, but the technological change is a matter prevalently managed inside the firm between undertakers – who oppose technology in the case of non profitability – and technicians, who are pushed by their instinct of workmanship to find new production systems, new products, etc. So institutional change is induced by conflict inside the firm although Veblen does not directly take the state of income distribution and its dynamic in this process into consideration. However it is important to notice that Veblen does not neglect the role of workers in institutional change. As also stressed by Walker (1977, p.230) in Veblen’s vision, machine discipline has a fundamental role in institutional change. In particular, machine discipline is the cause or revolutionary capacity of workers who – from a state of passivity and docility – modify their conception of institutions by a critical valuation of them. As Walker writes “[according to Veblen] participation of workers [in mechanical operations] induces them by occupational conditioning to think in the impersonal terms of causal sequences, and leads them to adopt scientific impersonality and mechanistic criteria in evaluating propositions. [Unlike technicians] workers begin to question the traditional metaphysical basis of justification of economics institutions. They become critical of specific economic and social arrangements, such as the distribution of income, the existence of privileged classes, the economic and legal domination of businessmen, thrift and even the family” (Walker, 1977, pp.230-231). More specifically, in chapter 9 of *The Theory of Business Enterprise* Veblen traces the lines for institutional change driven by workers; there are two main types of conduct: a) the conduct of workers, and b) the conduct of the labour union.

a) *The conduct of workers.* As it has often been written, workers work in strict contact with technicians and with the mechanical process; the social relationship that evolves between workers and technicians and the operative relationship that involves workers with machines has impacts on workers’ habits of thought. In fact technicians and machines act following the logic of the cause-effect relation that inevitably affects workers’ thoughts and behaviour. Such an influence does not preclude workers’ *free will*; on the contrary, matter of fact logic is seen as producing free will in workers in the sense that workers are trained to a critical scrutiny of the existing institutional order. In addition Veblen does not agree with the general idea that the contact of

workers with mechanical work lowers the worker's intelligence; he sees this idea as too radical a vision of the facts. As remarked by the author, the addiction to mechanical work lowers the intelligence in some respects but in other respects this addiction raises worker's intelligence. More specifically, mechanization reduces the intelligence for those tasks that were the responsibility of workers before the advent of mechanization, but it increases intelligence in the tasks for which mechanization has been introduced. The consequence of the process described produces a mental training of worker's habits of thought which oppose the existing institutions; consequently conflicts between workers and undertakers can occur in similar ways as conflicts between technicians and undertakers. If the result of such conflict favours workers then new technology is introduced into the system and if new technology is introduced then new institutions substitute the preceding ones. In addition and apart from the mental training to which workers are induced there is also a phenomenon of social mobility imposed by mechanization which assumes a particular relevance in a process of institutional change driven by workers. Veblen stresses that the labour force is in fact movable, interchangeable, and distributable in an impersonal manner like the parts of a mechanical system. In a context of strong social mobility it is not to the worker's advantage to have property and more specifically, real property. In fact a profitable investment in real property calls for continuous upkeep and improvements, but workers are not able to manage such investments because of the mobility imposed by the industrial system and because of the negligible or nil level of personal savings; not only are the savings insufficient for a profitable investment but the material impossibility of managing the investment discourages any savings. The issue of social mobility and its impact on property plays an important role in Veblen in the process of institutional change driven by workers. The consequence of social mobility - imposed by mechanization - is in fact a particular moral effect: i.e. workers lose the sense of ownership as a natural right and as a necessary source of well-being; Consequently if ownership loses its ethical recognition then the existing institutional order loses its validity and institutional changes are possible; also in this case the institutional order changes in response to changes in habits of thought.

b) *The conduct of the labour union.* Apart from the *current* negative management of the labour unions of his times Veblen continued to attribute an active role in the process of institutional change to the labour unions. As remarked by him, it

is no accident that the real development of the labour union took place in concomitance with the evolution of mechanization. The author argues that the “spirit” of the labour union is to beat the canons of ownership, of business aims and free contracts – with a particular mention to the labour contract and to the ‘private’ management of workers on the part of undertakers – when they are in contrast with the living conditions imposed on workers. Veblen stresses that when a given order is intolerable for the conditions of workers then the labour union starts its fight to modify the institutional order and when the conflict is in favour of labour unions then a new institutional order can arise; this new order can be more or less compatible with the institution of ownership and in the extreme case of a complete removal of the right of ownership, it can assume the form of a socialist or anarchic society. However, such a profound change for a wider spread of mechanical logic to all social classes which cannot have concrete realization in cases where large parts of social classes are excluded from the influence of mechanical logic. Hence, and according to Tilman (2003, p.xvi; italics added), the institution of industry in Veblen “has an emancipatory impact on the psyche of industrial workers which turns them against social convention and *presumably* in favour of socialism”. Some of the literature does not attach great importance to the Veblenian hypothesis of an active role of workers in institutional change. O’Hara for example remarks that “unlike Marx Veblen was not convinced of the endogenous movement toward progress through the underlying classes challenging the control of economic resources by the vested interests” (O’Hara, 2000, p.68). This belief was probably just motivated by the institutional context in which Veblen writes which was not in fact ready for a change induced by workers because:

“The underlying population is still very credulous about anything that is said or done in the name of Business, and there need be no apprehension of a mutinous outbreak, just yet” (Veblen 2001 [1921], p.70).

c) Institutional changes driven by changes in the dynamic of income distribution. It has been said above that in Veblenian thought conflict has a revolutionary aim in the sense that the existing social order and the order of ownership ‘rights’ could undergo a radical change driven by socialistic or anarchic movements. In view of the interpretation proposed here, it is suggested that institutional change is a change of habits of thought which aim is a ‘fair’ income distribution. In the interpretation

proposed here the revolutionary aim of the conflict may not develop if the State replies to the conflict by favouring the underlying population. In Veblen the conflict seems to produce radical changes in the social order since:

“It seldom happens, if at all, that the government of a civilized nation will persist in a course of action detrimental or not ostensibly subservient to the interests of the more conspicuous body of the community's business men” (Veblen, 1904, p.287).

But it will be argued that a policy in support of the popular claim favours the kept classes since they can maintain the existing social order. In particular, as will be shown, institutional change ultimately derives from the leisure class path of consumption. The following assumptions are in order:

a) the leisure class is interested in competitive and ostentatious consumption. The source of its income is financial rent driven by the money market and by financial market (see §§ 2.1 and 2.2.1);

b) firms are interested in obtaining money profits, which depends on the increase of prices via reduction of production (see §§ 1.4 and 2.2.2);

c) workers react to a fall in wages and the unemployed to the state of unemployment *via* social conflict. Moreover, the underlying population is composed of both employed and unemployed workers. The latter are assumed to receive unemployment benefits via the real aids granted by “charity organizations” (see Veblen, 1904, ch.10)⁸³. It will be argued that the social conflict will be generated both under conditions of full employment and under conditions of unemployment. In both the cases conflict can be brought into operation *before* or *after* the increase in rent and mainly on non-purely-rational bases⁸⁴. In addition, note that Veblenian social conflict

⁸³ Note the role of the charity organizations played a significant role during the 1800s. Historically charity organizations worked in the United States in the form of philanthropic institutions with the aim of supporting the poor, a large part of the community, and also the unemployed (see Barbeta and Maggio, 2002). In the description of the traits of the leisure class Veblen himself makes reference to the philanthropic behaviour of members of the leisure class. The consequence is that the leisure class – even if the same reasoning can be followed for the undertaking class (see Veblen, 1970 [1904], pp.69-70) – is not extraneous to completely unselfish solidaristic behaviour. It is not easy for Veblen to justify the leisure class's habit and proclivity to charity. In fact he refers to “alien motives” or as permanent “residue[s]” of a non predatory culture – “archaic traits” – that is to say “residues” that the canons of the leisure class are not able to crush (Veblen, 1975 [1899a], p.333-335).

⁸⁴ The distinction between full employment or unemployment is not incidental. In fact it has been seen in section 2.5 how rent can have positive or negative effects on production and employment. In particular it has been seen that when the system works in a condition of unemployment the increase of rent determines an increase in employment; so it could be argued that the increase of rent should not produce social discontent. In the course of our examination, it will be explained that – by the rereading of Veblen's works – it is possible to assume that the unemployed – but the same applies to workers – do

presupposes cohesion amongst workers as well as cohesion amongst the unemployed; this in fact is a sufficient condition to avoid free-riding behaviours. In fact as Veblen remarks for social conflict to be in operation and potentially successful “two main lines of subsidiary preparation” are to be considered: “(a) an extensive campaign of inquiry and publicity [...]; and (b) the working-out of a common understanding and a solidarity of sentiment between the technicians and the working force” (Veblen, 2001 [1921], p.103)⁸⁵.

The argument runs as follows. The individual members of the leisure class are involved in processes of competitive consumption. This means that individual *A* aims at obtaining a level of consumption higher than the level of consumption of individual *B* belonging to the same social group. It is worth noting that the leisure class as a whole is interested in preserving the existing social order and that this aim can be achieved *via* a level of conspicuous consumption consistent with no reaction on the part of workers and the unemployed, i.e. a level of wage and unemployment benefits which guarantee at least the level of consumption accepted by workers and unemployed. Otherwise, the individuals belonging to the leisure class want – on the microeconomic plane – to continuously increase their consumption. This mechanism produces the following effects. Since consumption on the part of the leisure class is guaranteed by financial rents, it acts in the monetary market by increasing the interest rate and in the financial market by purchasing large parcels of stocks and bonds; the financing cost for firms increases since firms have to pay more interest and dividends to the leisure class; so the tendency to increase consumption, that is to say waste, generates a tendency to increase financial costs, and therefore financial rent. Since financing costs are increasing, firms react by raising prices in order not to lose profits, or – if they cannot exploit this strategy due to a lack of demand – to reduce investments. Price increases determine a reduction of real wages, and the reduction of investments determines a drop in output; the reduction of output in turn produces

not know, and cannot know, the effects of an increase of rent on employment; at the same time the unemployed – and workers also – act on irrational bases so they may enter into conflict anticipating and neutralizing the Malthusian effect (§ 2.5). Moreover it will also be explained how in Veblen the neutralization of the Malthusian effect does not invalidate the possibility of economic growth.

⁸⁵ In addition since the underlying population is naturally solidaristic the possible coordination between workers and unemployed can be admitted; so it is reasonable to think that the social conflict starts at the same time from workers and the unemployed.

negative effects since: *a)* it again increases prices and reduces real wages and *b)* it again reduces employment.

An increase in waste therefore pushes the system to work with a reduction of real wages; such a reduction determines a negative gap between the real wage and the exogenous subsistence wage; the higher the waste, the higher this gap. If the undertakers can neutralize the increase of financing costs *via* the increase in prices or new capitalization then the rents/profits rate can be maintained unchanged⁸⁶; on the other hand the increase in prices or disinvestments enlarge the gap between rents and wages. A question may now arise: what – if any – is the limit to the growth of the rents/wages ratio? Rereading Veblen it is possible to say that the rents/wages ratio can increase until workers and the unemployed can no longer tolerate such growth. In other words the increase of rents/wages rate has a limit of endurance for workers and the unemployed and Veblen calls this limit the “limit of tolerance” (Veblen 2001 [1921], p.12).

Veblen generally refers to the limit of tolerance to indicate a given condition of endurance of the state of things beyond which popular discontent emerges. As he writes:

“Social structure changes, develops, adapts itself to *an altered* situation, *only* through a change in the habits of thought. [The] evolution of society is substantially a process of mental adaptation on the part of individuals under the stress of circumstances which will *no longer tolerate* habits of thought formed under and conforming to a different set of circumstances in the past” (Veblen, 1975 [1899a], p.192).

More specifically, the limit of tolerance is affected by employment conditions and by whether the subsistence wage received is congruous with the “necessities of life” (Veblen 2001 [1921], p.12). As Veblen remarks:

“It is more particularly in times of popular distress [...] when the *current output of goods is not nearly sufficient to cover the consumptive needs of the community*, that considerations of business strategy calls for a wise *unemployment* of equipment and man power is the most *obvious* cause of *popular distress*” (Veblen, 2001 [1921], p.71; italics added).

⁸⁶ See section 2.2.2 which explains how capitalization produces profits in Veblen.

When the workers' necessities of life are covered by the subsistence wage, i.e. when production is maintained at a high level that also assures employment, then no popular distress is generated. On the other hand, when the subsistence wage is lower than the necessities of life, i.e. when production is maintained at a low level that also determines unemployment, then "popular distress" or "popular irritation" (Veblen, 2001 [1921], p.66) arises. Popular distress – both for workers and the unemployed – is therefore a consequence of high prices or disinvestments which in turn is a consequence of the increase of financial rents, in view of the causal links existing between rent increases, disinvestments (or increase in prices) and low wages and unemployment. Popular discontent as regards the rent/wage rate takes various forms and its intensity depends on the proximity of this distress to a limit of tolerance. So in a given institutional context a distribution of income in favour of the kept classes is subject to a limit of tolerance for workers and unemployed.

Although Veblen does not directly address the question - arguing that the "limit of tolerance [is] a hazardous topic of speculation" (Veblen, 2001 [1921], p.76) - the issue of the determinants of the limit of tolerance should be subject to a more detailed inquiry. It is reasonable to think that the limit of tolerance is measured differently for workers and unemployed. With reference to workers their own limit of tolerance is measured in terms of maximum difference tolerated between the real wage received and the subsistence wage desired, assuming this limit as exogenous data⁸⁷; at the same time the limit of tolerance for the unemployed is measured in terms of intensity of unemployment produced by reduction of output, and also this limit is considered here – for the sake of simplicity – as exogenous data. When the limit of tolerance has been reached the next question is the investigation of the consequences deriving from it. In other words, the question is: what happens when the material conditions of the underlying population reaches the limit of tolerance? Rereading Veblen it is possible to argue that when the limit of tolerance is reached, social conflict becomes highly probable. As Veblen writes:

⁸⁷ It is interesting to note that this interpretation appears to be in line also with Keynes's view of social conflict. In Keynes social conflict is generated when wages are reduced to "an extreme degree". As Keynes writes: "it would be impracticable to resist every reduction of real wages, due to a change in the purchasing-power of money which affects all workers alike; and in fact reductions of real wages arising in this way are not as a rule resisted unless they proceed to an extreme degree" and the reduction in wages disturbs political confidence, by causing popular discontent" (Keynes, 1973 [1936b], p.264).

“Something in the nature of *riotous discontent* and *factional disorder* is perhaps to be looked for in the near future in this country, and there may even be some *rash gesture of revolt* on the part of ill-advised malcontents. *Circumstances would seem to favor something of the kind*. It is *conservatively estimated* that there is already a season of privation and uncertainty in prospect for the underlying population, which *could be averted* only at the cost of some substantial interference with the vested rights of the country's business men, - *which should seem a highly improbable alternative*, in view of that spirit of filial piety with which the public officials guard the prerogatives of business as usual” (Veblen, 2001 [1921], p.64; italics added).

When the limit of tolerance is reached a problem arises: on what grounds does the underlying population decide to start the conflict? Theoretically there are two possibilities: *a)* the conflict is brought into operation *via* economic grounds, in other words on rational grounds, or *b)* the conflict is started *via* moral grounds - the “unreasoning sentiment” (Veblen, 1904, p.288) - in other words on irrational grounds. In Veblen the conflict has no economic basis but only a moral one and this occurs for two main reasons. First, the idea of the rationality of conflict presupposes that agents are able to calculate the present costs and, above, all, the expected benefits. In a context of uncertainty, as Veblen considers a capitalist economy, this calculus is impossible. Second, as argued above (see §§ 1.1 and 1.2), agents behave according to instincts, so that the possibility of a rational action is to be excluded on the methodological plane. As pointed out by Veblen, the outcome of social conflict - i.e. mainly involving changes in the formal laws and the Constitution (particularly, "the clause which specially safeguards the security [of absentee ownership]" - appears to be uncertain, since it is not known "*if and when*" this change will occur (Veblen, 1921, p.99, italics added). Even though the outcome of conflict is uncertain, its costs are known. In particular the certain cost of the conflict for workers is the loss of wages while the certain cost for the unemployed is the loss of subsistence guaranteed by charity organizations. Since costs are known but the benefits are uncertain, workers and the unemployed cannot act on economic grounds; the consequence is that their action is not rational. Veblen assumes that – in line with his theory of economic behaviour alternative to the neoclassical vision (§§ 1.1 and 1.2) – the dimension of conflict therefore cannot be economic but moral.

More specifically in the moral dimension workers and the unemployed are hit by a sentiment by which they judge the existing institution as ‘unjust’ as regards a decent livelihood which in Veblen’s words becomes a “universal, and universally

laudable, ambition of all who have reached years of discretion” (Veblen, 2001 [1921], p.100). On this point he writes:

“There has lately been some *irritation and faultfinding* with what is called “profiteering” and there may be more or less *uneasy discontent* with what *is felt* to be an *unduly disproportionate inequality* in the present distribution of income” (Veblen, 2001 [1921], pp.99-100; italics added).

Moreover, Veblen argues that the moral dimension of the limit of tolerance is shown when workers perceive that they have “nothing to lose” even if their wages are not nil, just as the unemployed perceive that they have nothing to lose even if their aid is not nil. This is to say that social conflict is not a purely *rational* reaction, but involves an ethical consideration on the criteria underlying the existing income distribution. As Veblen writes in his “*The Engineers and Price System*”:

“The underlying population *would have anything to lose* by such an overturn of the established order as would cancel the vested rights of privilege and property” (Veblen, 2001 [1921], p.61; italics added).

In addition in his “*The Socialist Economics of Karl Marx and His Followers*” (1906) Veblen writes:

“There is [...] *not even a direct causal connection* between the material forces in the case and the choice of a given *interested line of conduct*. The attitude of the interested party does not result from the material forces so immediately as to place it within the relation of direct cause as effect, nor even with such a degree of intimacy as to admit of its being classed as a tropismatic, or even instinctive, response to the impact of the material force in question. *The sequence of reflection, and the consequent choice of sides to a quarrel, run entirely alongside of the range of material facts concerned*” (Veblen, 1906b, p.582-583; italics added).

The above passage is useful in clarifying the moral dimension of the limit of tolerance. In fact rereading the above passage it is possible to say that material matters – such as the decreasing of the real wage and the increase in unemployment – quantify the limit of tolerance but they do not explain its origin which is moral and not economic. If the moral dimension of the limit of tolerance is precisely the dimension by which the propensity to conflict is ruled, then a problem left unclarified by Veblen is the moral reasons why workers and the unemployed might start a conflict; in other words the

moral logic of social conflicts is not clear in Veblen. Social philosophy has historically divided the reasons for social conflicts with three categories, honour, glory and prestige. These categories – according to Honneth (1992, p.189) – are connected to the objective distribution of life opportunities amongst members of the collectivity and the moral sentiments or the moral stress are not taken into consideration. In other words the above categories in fact have an economic basis since they reflect losses connected to the acquired ‘rights’ but they not reflect the moral sentiment and the moral stress of the loss suffered. In Honneth’s work the main moral sentiment or moral stress that pushes a social group to clash with other groups is the sentiment of stress that origins from non-recognition and non-appreciation. In other words given a collectivity composed of two groups (*A* and *B*), when the effects of the actions of group *A* lead *A* to remove recognition and appreciation from *B*, then this underestimation determines stress in *B*. Accordingly, each social group is constantly fighting to obtain social esteem from others; in brief – according to Honneth – the object of social conflict is not mainly economic, for example the distribution of resources – but mainly non economic and it consists of social esteem as a value in itself. Even if Honneth is not a scholar of Veblen his work can help us in rereading Veblen on the moral dimension of the limit of tolerance. Honneth in fact is a scholar of the Hegelian philosophy on social conflict and he develops his theory through a rereading of Hegel (see Fabrizio, 2006) and Veblen probably builds his theory of conflict having in mind the Hegelian theory. As Veblen writes:

“The struggle which constitutes the method of [...] evolution is, in the Hegelian system proper, the struggle of the spirit for self-realization” (Veblen, 1906b, p.580).

Recognition and appreciation can be seen as conventional factors – historically contextualized – by which each social class is identified from others. So recognition and appreciation is first of all a matter of habits of thought; as a consequence, social esteem is primarily a question of habits of thought. At the same time Veblen emphasises the fact that the social esteem of *his times* is based on wealth owned: the greater the wealth, the higher the esteem. When the wealth of a social group suffers a reduction then the group itself is damaged in its recognition and appreciation; so the consequence of a reduction in wealth determined by one social class automatically highlights the underestimation of another one. The outrage of the class involved in a

process of profiteering to the detriment of others is not so much in the removal of the wealth as such, but in the implicit and unexpressed intent to underestimate other classes, in other words in the intent to remove esteem from others. In these terms conflicts do not find directly originate in the struggle for existence but in the struggle for recognition, and therefore in the struggle for esteem. If a social class does not 'deserve' to be recognized and appreciated, so if the social class *A* conventionally - for a matter of habits of thought - does not attribute esteem to another one (*B*) then no moral impediment can stop the predatory behaviour of *A* on *B*. In other words, because of habits of thought of the leisure class the underlying population is an unworthy class (see ch.1) so the underlying population or the unemployed do not deserve esteem; so members of the leisure class do not attribute a worthy role to the underlying population and if the underlying population is an unworthy class then it does not deserve recognition and appreciation. Note that it is reasonable to think that in Veblen social conflict is not driven by envy for two main reasons: *a*) Veblen attributes the sentiment of envy to the leisure class, not to workers or the unemployed, *b*) it is reasonable to think that if envy were the source of social conflict than the Veblenian idea of a coexistence of different habits of thought would disappear and all human behaviour would be motivated by predation. An immediate way of underestimating or intensifying the underestimation of the underlying population is to reduce its source of income; the consequence is that the variation in favour of the leisure class of the rents-wages rate becomes the evidence of the implicit intent of the kept classes to underestimate the underlying population. The limit of tolerance is reached when the divergence between rent and wages is perceived by the underlying population as intolerable evidence of the process of underestimation perpetrated by the leisure class. The perception of the intolerable action of underestimating by the leisure class is a cultural matter; so the limit of tolerance is reached when the underlying population develops a group consciousness of its own sentiment of recognition and appreciation and on the intolerable action of its annihilation committed by the leisure class. As Veblen writes:

"The principles and practise of the distribution of wealth vary with [...] *the [...] cultural changes [...]*; but it is probably safe to assume that [...] the consensus of habitual opinion as to what is right and good in the distribution of product [...] have always been such as to give one person or class something of a settled preference above another (Veblen 1908b, p.113, italics added). Principles

(habits of thought) countenancing some forms of class or personal preference in the distribution of income are to be found incorporated in the *moral code* of all known civilizations and embodied in some form of institution” (Veblen, 1908, pp.112-113, italics added).

The final point of investigation on the limit of tolerance and social conflict is about the effects of the conflict generated. More specifically several effects can occur which can be classified into: *a*) effects on the institutional plane; *b*) effects on the macroeconomic equilibrium.

Let us see the effects on the institutional plane. When the limit of tolerance has been reached the existing income distribution is recognized as ‘unfair’. The recognition of the income distribution as ‘unfair’ requires a change in the habit of thought; so the underlying population starts to think in critical terms about the existing state of things and in particular about the existing order of income distribution. Passivity and docility of thought of the underlying population is replaced by a critical reasoning similar to the matter of fact logic based on the following logic chain: since the *consequence* of the existing distributive income is equal to the underestimation of the underlying population then the *cause* – that is to say the existing distributive order – needs change.

If the underlying population perceives the income distribution as ‘unfair’, then it perceives the habits of thought of the leisure class as a negative value, but if it perceives the habits of thought of the leisure class as a negative value then it accepts workmanship as a value in itself. However even if the underlying population conceives the habits of thought of the leisure class as negative values and workmanship as a value this does not mean that the worker’s productivity necessarily increases (cf. Walker, 1977). This detail is useful in pointing out that on the macroeconomic plane, economic growth is not a simple consequence of the acquisition of a habit of thought⁸⁸.

On the macroeconomic plane in fact, the behaviour of the State plays a fundamental role in economic growth and the maintenance of the existing institutional

⁸⁸ If we wanted to reread the Walker’s interpretation (see above) we should reasonably say that now workmanship rules the behaviour of members of the underlying population just as workmanship affects the behaviour of technicians, and since workmanship is the attitude to efficiency, to production and to the accumulation of knowledge for production, then it is reasonable to think that conflict generated by an ‘unfair’ income distribution leads the system towards a path of economic growth since the under utilization of capital is now conceived as waste and workers act for the full utilization of the capital which in turn increases the level of employment.

order. In fact if the State reacts to the social conflict by repressing it then popular discontent can reasonably be expected to rise; the harsher the repression, the greater the likelihood of institutional change. Note that a repressive action of social conflict is counterproductive for the leisure class. In fact if the leisure class opposes a fairer income distribution, so if it continually enlarges the gap between rent and wages without resorting to policies of re-equilibrium of incomes then it is reasonable to think that the underlying population can be pushed towards conflictual actions. On the other hand, the taxation of rents produces a double positive effect: *a)* one in favour of the leisure class although not directly demanded by it and *b)* a one in favour of the underlying population. In other words the collectivity as a whole would obtain benefits if a policy of taxation of rents were used by the State. Let us see why: Starting from a condition of unemployment, the increase in wages – derived from reduction of rents *via* their taxation – increases total demand. Businessmen are likely to react *via* the reduction of the degree of under-utilization of capital and, hence, increasing labour demand. Since more capital and more labour are now employed, the aggregate output increases as does the rate of growth. Therefore, *social conflict – if it is successful – is an effective means of increasing employment and the rate of growth*⁸⁹. At the same time the underlying population has no reason to oppose the existing social order since wages and employment increase. The leisure class can therefore continue to be the ‘primary’ social class and the existing institutional order can be guaranteed. In conclusion it is possible to note that *a distributive dynamic in favour of the leisure class tends to produce effects contrary to it if no policy of re-equilibrium of income exists*. Note that starting from a state of unemployment, an increase in rent at any rate produces – thanks to the Malthusian element in Veblen – production and employment (see § 2.5) but, at the same time, it determines institutional change. On the other hand, if the income distribution is ‘fairer’, production and employment increase but institutions may be maintained over time. Finally, note that in a condition of full employment an increase in rent only produces negative effects on the institutional and economic plane. In fact if rent increases, prices increase and real wages decrease: so conflict starts; if rents are taxed then wages increase; when wages increase demand increases too but given the condition of full employment only prices can increase

⁸⁹ Note that if wages increase undertakers may react by dismissing workers. If undertakers react with dismissals, then production falls and prices increase; the consequences are that unemployment increases and real wages decrease. Since rents are increasing, – due to the Malthusian element (see § 2.5) – demand may not suffer decreases but the conflict does not stop.

again and a process of inflation is generated. However, if rents are not taxed, conflict is not stopped and the effect is institutional change combined with inflation.

CONCLUDING REMARKS

The “ironic structure in Veblen’s writings” is widely recognized (Cassano, 2005), and this is one of the main problems in the interpretation of his thought. In recent times there has been a renewed interest in Veblen’s economics, and this work falls within this line of research. Its main purpose is to focus on Veblen’s theory of income distribution, economic growth and institutional change, in the attempt to furnish an organic description and interpretation of his works. In particular, various related topics have been discussed in the previous chapters: employment, income distribution, economic growth and institutional change. These topics have been studied within an environmental context featuring conflicts originating from the struggle between instincts and habits of thought and intensified by the predominance of a money culture. We have first of all tried to bring order to the Veblenian theories of instincts and institutions regrouping them as typical traits of the Veblenian social classes: leisure class, undertakers, technicians and workers. Predation *vs.* workmanship and ownership *vs.* industry have been seen as sources of incompatibility and conflict between the aims and actions of social classes. Employment, production and development are thus the outcome of conflicts between incompatible instincts and institutions. This certainly confers originality on Veblen’s thought since he tries to find the origins of economic matters in non economic matters. So employment, production and development do not have an economic origin but an institutional one. Availability of resources, productivity of inputs, prices, demand, employment etc, are not the substance of economic choices and actions but the effects of human proclivities. ‘Good’ proclivities – workmanship, idle curiosity and parental bent – can therefore support the economy and ‘bad’ proclivities can depress it. Starting from such a global vision of Veblen and his thought, the work has then tried to show a possible reconstruction and reinterpretation of Veblen’s view of the process of generating unemployment. It has been shown that the level of employment is the result of internal conflict of firm, or rather as the result of conflict between undertakers and technicians. undertakers – due to a predatory instinct - want to reduce production in order to keep prices high and obtain high monetary profits, while technicians – due to an instinct of workmanship – want to keep production high. In fact employment is a function of the

degree of utilization of capital, which is reduced if the undertakers' profit aim overcomes the technicians' production aim. Moreover, given the context of credit economy and an economy ruled by competitive consumption, the leisure class continuously pursues increases in financial rent by increasing interest rates and buying stocks and bonds. This can generate two effects: *a)* when financial rent increases the leisure class increases its demand for goods; this in turn generates an increase in investments, production and employment (*Malthusian element of Veblen*); *b)* at the same time financial rent is a financing cost for firms anyway and when full employment is reached, there is an additional increase in rent, reduced profits, increased prices, reduced real wages. The reduction of profits combined with the reduction of the real wage determines a reduction in investment, production and employment; investments in fact are affected negatively by the high costs of financing and by the negative expectations on sales. This kind of unemployment has been called *unemployment from external conflict*, since it derives from the conflict in the distribution of income between social classes. Finally the rereading proposed here has also suggested the idea that institutional change is driven by the dynamics of income distribution. The key variable is the limit of tolerance of workers and of the unemployed concerning their real wage level and state of unemployment. Both the workers and the unemployed can therefore suffer the state of a distribution of income by the leisure class when this reduces the real wage and employment; when the limit is reached, social conflict occurs. In addition it has been shown that the grounds for social conflict are moral and not economic in Veblen since the economic basis of the conflict calls for a rational calculus on expected benefits and costs of conflict which the Veblenian agent in fact is not able to make. Moreover social conflict, in turn, affects habits of thought, in the sense that workers and the unemployed internalise critical attitudes towards the existing social order and perceive waste as a non value (and, by contrast, efficiency as a value). Moreover, the social conflict not only determines institutional change but also economic growth. In fact social conflict pushes the system to distribute income more equally. In other words social conflict determines an increase in real wages; when real wages increase total demand increases and undertakers are more inclined to increase the degree of utilization of capital by employing more workers.

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