Economic Power and the Real World: A Post-Keynesian Analysis of Power

Virginie Monvoisin & Louis-Philippe Rochon


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The analysis of power has a long history in the annals of the social sciences. It is central to the understanding of human interactions and the evolution of social conditions and institutions. In most disciplines, it holds a central place in the discourse and is ingrained in the development of ideas.

As in other disciplines, the notion of power is central to economics—or rather it should be. Strangely enough, there is an uncomfortable divorce between the concept of power on the one hand and the study of economics on the other. Indeed, most—if not all—disciplines in the social sciences account for the exercise of power over the most fundamental of human conditions. In economics, however, very little is said about it, and even less on how it can be woven into an overall theory of capitalist markets. This criticism applies principally to neoclassical theory, although it can certainly be applied to many heterodox approaches as well.

In fact, we could argue that economics, a discipline that relies on the study of finance, money, production, and a host of various
agents, embodies in its current state the very absence of power. Heilbroner made that pointedly clear in reviewing the publication of the *New Palgrave: A Dictionary of Economics*, which, he observed, has no entry “on power, although power should seem to be inextricable from economics” (1988: 23). This is not surprising. The dominance of neoclassical theory has somehow convinced many that power is nonexistent or simply not worth discussing.¹

Yet just because neoclassical and other approaches do not directly acknowledge the existence of power does not mean of course that power does not exist. To paraphrase Keynes’s (1973 [1936]) analogy of the long run, it seems that neoclassical economists really are interested in merely studying the ocean after the storm; they ignore the fact that there are important water currents under the surface of the sea that influence the dynamic nature of the ocean. The surface may be calm, but it hides something quite different.

The fundamental question, therefore, is how do we incorporate the concept of power within economic theory, and, certainly just as important, how does economic policy account for it?

In this paper, we do not wish to get into a semantic debate over the precise nature of power. Such debates are best left to political scientists or philosophers. As a first step, however, we accept a very general, Weberian definition of power. Here, we define power, within the sphere of economic analysis, simply as the ability of one economic agent (the State, the firm, or even a household) to impose his or her state of preferences on others for economic gain.² Alternatively, power is the ability to secure the necessary resources—or access to these resources—(financial in particular but also legal, for instance), to impose one’s own point of view on others. Of course, the greater the resources, or access to these resources, the greater is one’s power. In a sense, we abide by a widely accepted definition of “confictual power.” Hence, according to Scott, power arises “whenever A affects B in a manner that is contrary to B’s interests. Such an approach sees power as asymmetrical: they are zero-sum relations which involve actions in which there is potential resistance or conflict between agents” (1994: 2).

To be fair, of course, some heterodox approaches do discuss the
notion of power. For instance, Marxists (see, e.g., Bowles and Gintis 1994) and institutionalists (in the Galbraithian tradition, see Kesting 2005 but also Bartlett 1994; Veblen 1904) in particular have long recognized the importance of power and market economies.

Yet, these approaches all discuss how power is exercised—not how power arises or rather why power exists. Although we agree with much of the Marxist and institutionalist literature on power, which tacitly recognizes the importance of social classes and class struggle, our own approach is rather different. To explain the existence of power, however, we believe that post-Keynesian theory, among all other heterodox traditions, is best placed to answer this question.

We therefore propose a theory of power from a post-Keynesian perspective and wish to explain foremost why power exists, not simply how it is exercised. In some ways, this is also a critique of classical economics, which aims to explain power through class struggles over the appropriate division of the surplus. However, this simply tells us how power is exercised ex post, that is, after production takes place. In a sense, what we want to do here is to look at power ex ante, that is, during the production process itself, and seek to explain why there is power to begin with. This approach inextricably explains why power is also not discussed in neoclassical theory.

The principal focus of this paper therefore is to see if it is possible, from a post-Keynesian perspective, to incorporate power within an economic analysis of production. To be successful, we must combine the notion of power with some of the more fundamental tenets of post-Keynesian theory. In this respect, we link the existence of power (and hence why it exists) to two crucial elements of post-Keynesian analysis. First, we argue that, for power to exist, there must be a proper hierarchy of agents in the economic structure and, as such, an important asymmetry between economic agents. This aspect is often emphasized in many accounts of class struggle.

Second, and more important, we believe that for power to exist we must live in a nonergodic world—that is, a world with uncer-
tainty, à la Davidson (1996), defined as the absence of knowledge of future events. Hence, we argue that it is the presence of uncertainty that leads agents to try and secure a greater portion of the distribution of income. Given their hierarchy in the economic order, agents will be successful to various degrees. In this sense, it is to Davidson that we owe a collective debt and hence the inspiration behind the title of this paper.

If this view is correct, then we understand why neoclassical theorists are unable to account for power, because they assume a perfectly ergodic world. When neoclassical economists do deal with power—albeit superficially—it is usually tied to the existence of an imperfection, which leads to suboptimal results.

For post-Keynesians, however, the exercise of power is not the result of an imperfection; rather it is a normal (or common, or permanent) feature of economic life. Lavoie is one of the only post-Keynesians (to our knowledge) who addresses the issue directly. Interestingly enough, he also links power to uncertainty, although the concept is never developed beyond the mere mention of it: “The firm wants power over its suppliers of materials, over its customers, over the government, over the kind of technology to be put in use. . . . In a world without uncertainty, the notion of power dissolves and loses much of its importance” (1992: 99–100).

The notion of power is thus tied directly to uncertainty. If this is correct, then it is also tied to the notion of effective demand: It is the uncertainty over the level (or growth) of effective demand in the near future—and its implications for all agents in the economy—that makes the notion of power such an important component of economic analysis.

**From Classical to Neoclassical Economics: Power and Markets**

For the authors of the surplus approach—in particular Adam Smith, David Ricardo, and Karl Marx—the accumulation of capital was the main focus of analysis. The fundamental issue was the expla-
nation of how the economic system reproduced itself on an extended scale and how it could grow through time. Essentially, the production of output needed to be sufficient enough to replace the inputs used in the production process, thereby guaranteeing the ability of the system to maintain its current level of production and reproduce itself. Any output over and above the inputs, called the surplus, could then be divided between the various social classes involved in the production of commodities. There is, however, the possibility of conflict over the precise distribution of the surplus, which in turn is associated with the growth of the system in the future.

The conflict arises because each social class (workers, capitalists, and rentiers) wants to extract from the surplus the biggest share for itself. Although workers produced the goods, they must sell their labor force to subsist; capitalists own machinery or the means of production; and rentiers (or landlords) rent the land on which the machines are used. In turn, each social class draws an income from their relative position in the production sphere: (subsistence) wages for workers, profits for capitalists, and rents for the rentiers. As such, the economic system recognizes and acknowledges the specific role of each social class: The classical system is a highly hierarchical system of production on which rests the theoretical determination of the labor theory of value and prices. Indeed, the exchange value of the goods depends first of all on the quantity of work necessary to produce them and thus on the working class, whereas the price depends on the wages, profits, and rents. Each income is subject to its own laws, at times contradictory and thus sources of conflicts—Malthus’s “principle of population” or Marx’s famous exploitation of the working class. Also consider Ricardo’s law of decreasing returns (which applies to rents), and Ricardo’s and Marx’s laws governing accumulation, applying to profits.

Provided workers consume all their wages (excluding rents accruing to land owners), the surplus goes to the capitalists, which they use for their own consumption necessities and for increasing the scale of production in the following period (investment). If
reproduction only requires the replacement of the inputs, growth arises out of investing more than the quantity of initial inputs. For the classical political economists, the higher the surplus, the higher the possibilities of raising the rate of accumulation of capital and the higher the possibility for economic growth and the creation of wealth in the future. Power over the distribution of the surplus was a key element of the survival and growth of the capitalist class.

With the rise of the marginalist revolution of Jevons, Menger, and Walras, however, neoclassical theory discarded the emphasis on social classes. In Jevons’s words, the purpose of the marginalist revolution was to “fling aside, once and for ever, the mazy and preposterous assumptions of the Ricardian School” (1871: xiv). In its stead, it placed the individual at the heart of economic analysis. In this sense, if economic theory emphasized the atomistic individual—or what economic theory calls the representative agent—who all share the same objective irrespective of the social class to which he or she belonged, then there can be no conflict. Economic theory thus became a relationship between the individual and his or her needs and the identification of economic behavior with individual choice.

Neoclassical theory was thus born without references to class consciousness—that is, without any references to authority, social groups, or the existence of hierarchy in the production process. The emphasis rather was placed on the (rational) atomistic individual, on perfectly competitive firms unable to exert any authority over prices or output. Markets now took central stage. The new objective of economics was efficiency: “the efficient allocation of scarce resources.” Prices were determined by supply and demand within specific markets, and no single firm, in a purely competitive environment, was able to influence the price of its good. For that matter, workers also were unable to exert power over wages: They were simply paid according to their marginal contribution to production in well-organized labor markets. There were no unions or organized labor movement; if there were, these were imperfections that obscured optimizing the best solutions and distorted market prices and wages.
Markets are devoid of any references to institutions, history, or politics. They operate in an institutional void. The objective of neoclassical theory is therefore to develop “universal laws,” applicable to all time periods, in all circumstances, and, indeed, to all forms of market structures. Thus, neoclassical theory leaves all “human facts” to the political scientists or historians. As Say once wrote: “Political economy [economics] is not politics. It does not deal with distribution or the balance of power” (1821: 1).

One could argue that economic theory aimed at explaining power away. In a “perfect” world (perfect competition), there is no need for power. Any exercise of power only impedes market forces. The purpose of economics becomes purely a matter of optimization. The “representative agent,” which is used to describe either a firm or a household, maximizes either profits or utility, thereby allowing households to make decisions outside of all consideration of their relative social standing. Because of the marginal product of agents, the value of output is thus divided among the various atomistic agents in a power-free environment.

Here, there is no place for uncertainty. Provided agents obey the laws of marginal products, outcomes are known with certainty: There is only one possible optimal solution. In other words, equilibrium is unique. Even in those circumstances in which uncertainty is introduced, it is reduced to a probabilistic distribution.

Neoclassical theory is thus fundamentally atomistic. It relies on the supremacy of individuals and the interactions among them. There is therefore no real need to ground our analysis in macro-economics; this is seen merely as an aggregative exercise, that is, an aggregation of the behavior of atomistic agents. There is no discussion of social classes and no need to develop an independent macroeconomic analysis. Indeed, if all agents are alike, then the macroeconomy looks just like the microeconomy.

In this sense, the emphasis on perfectly competitive markets is made precisely to undermine the ability of any agent (firms) to influence prices or output. The concept of power is thus reduced or absent altogether from economic analysis. This is certainly not an original insight. After all, John Kenneth Galbraith made such a
statement over three decades ago. According to Galbraith, “the most commonplace features of neoclassical and neo-Keynesian economics are the assumptions by which power, and therewith political content, is removed from the subject” (1973: 2). In a way, we could argue that classical political economy transformed itself into “economic science.” According to Dockès,

the paradox is that economic science developed itself by radically abandoning any discussion of power. It is more than a mere question of a lapse of memory, but rather it is a conscious decision to build a physical-mathematical science. This is carried out in two stages: first, by the construction of . . . a perfectly competitive model; second, from this model, economists introduce particular cases corresponding to the other market structures. (1999: 3)

The economy, considered as a hard science, excludes a priori any serious discussion over the positions held by the agents because what is important is the allocation of scarce wealth, as well as how the market is organized according to very specific laws and rational behavior. Only prices bind agents, not social relations. Indeed, such an approach, based on the search for mathematical laws—that are as abstract as they are immutable—clashes with the ambiguities generated by the various social, political, and historical problems that arise when considering the exercise of power. Of course, these ambiguities cannot be explained through mathematical formulas.

Hence, the absence of power in neoclassical theory is reached by eliminating two important concepts: social conflict and uncertainty. Indeed, neoclassical theory emphasizes two related themes: the elimination of social classes and the rise of the atomistic agent, and optimization, which is done outside the existence of uncertainty. If there is uncertainty, it is reduced to probabilistic distributions.

Yet despite Say’s (1821) claim, neoclassical theory, and economics in general, cannot escape from the need to address the exercise of power. Attempts at camouflaging the existence of institutions, uncertainty, or social classes are not realistic and amount to reducing economics to a few behavioral laws. Also, because economics exists within the real world, it cannot be disassociated
from it, which is characterized by uneven relationships, powerful interests, money, and an unknown future. As Allais wrote, “economics, like all other sciences, cannot avoid dogmatism, but in economics dogmatism is considerably reinforced by the power of interest and ideology” (1968: 27).

Neoclassical economists, or at least some of them, are keenly aware of this, and it is in this sense that neoclassical theory has attempted to deal with the real world by introducing new elements to their analysis, without really distorting the foundational structure. This is the familiar separation between short-run and long-run analysis. Yet each time, these new elements are introduced as imperfections. The real world is seen as not living up to the theoretical model—the rebuke of the parallel lines, as Keynes (1973 [1936]) tells us. As such, these imperfections obscure the final optimal solution.

In game theory, for instance, uncooperative behavior is the purpose of the exchange. Agents make decisions without consulting each other. Yet, given the interdependence among agents, they are able to exercise some limited power. Thus game theory applies to situations in which markets are not purely atomistic but also in situations of duopolies. Agents then adopt strategic behavior: In fact they are forced to study all possible situations and develop strategies in a typical dominant–dominated environment. Given the absence of knowledge of how the other agents will act, the objective is to maximize one’s own satisfaction. The end solution is often suboptimal.

We therefore appreciate the consequences of allowing some, although very limited, exercise of power within an otherwise neoclassical structure: suboptimal solutions. Thus any references to possible dominant–dominated social relations cannot lead to the efficient allocation of resources.

Consider another example. In situations of asymmetric information, under conditions of adverse selection, one agent in the transaction process possesses more information than the other, as in Akerlof’s classic lemon (used car) market. This situation leads to fewer “good” cars being sold and to an abundance of “bad”
cars. In other words, the quality of the remaining pool of cars diminishes. The resulting suboptimal solutions are the result of the “uncertainty” in the contract or the transaction.

The same principle applies to labor markets. For instance, in the efficiency-wage literature and shirking models, management cannot know with certainty if workers are working or shirking their responsibilities. The solution is again a suboptimal solution: to offer higher-than-market real wages to encourage workers to work more and shirk less. The ultimate solution is to threaten layoffs. Asymmetric information can also impose considerable transaction costs. As a result, the firms must absorb these costs and in addition must develop a structure—give itself a hierarchy—to limit growing costs (Dupuys and Maris 1996: 3).

As diverse as these examples are, the end results are similar. First, whenever the neoclassical model attempts to stray from its pure competitive model, any assumption of unequal agents leads to suboptimal solutions. This shows that any whisper of power or its exercise is an imperfection. Second, straying even a bit from the perfect competitive model leads to a collapse of the most fundamental assumptions of the model. Once one realizes that agents may not be equal—that one agent can impose his or her preferences or conditions on the dynamics of transactions and trade—then any recognition of a dominant–dominated relationship should lead to a rejection of the model. Such relationships imply a specific hierarchy and the adoption of an institutional framework to deal with power. Finally, irrespective of the situation, neoclassical theory does not explain why certain agents have more power, why there exists asymmetric positions or situations, or why indeed agents are faced with uncertain situations.

Nevertheless, the framework of neoclassical microeconomic analysis remains very limited. A more thorough analysis requires a larger frame of analysis than the market. This is why we need to take the analysis to the realm of macroeconomics. Only there can we offer a proper analysis of uncertainty, effective demand, power, and hierarchy.
François Perroux, Power, and the Hierarchy of Agents

The previous section discussed, though briefly, the importance power plays in classical and neoclassical theories. As was argued above, the dominant economic paradigm appears unable to analyze properly the notion of power, and although its recent developments are intended to study the asymmetry of agents’ positions, it nevertheless seems unable to explain the causes of them. Moreover, it supposes that such situations seldom have harmful consequences—except in situations of adverse selection—because it is always possible to return to a position of equilibrium.

We propose in this section one of two possible criticisms to this approach. Heterodox economists can fall back on the work of French economist François Perroux (1961). Yet his approach, as we argue, leaves us unsatisfied. Our second choice, explored and developed in the next section, is to turn to the post-Keynesians and their emphasis on asymmetrical relations and uncertainty.

Although Galbraith (1973) was a leading institutionalist critic of neoclassical theory in Canada and the United States, François Perroux (1961) and his followers in France provided in many respects a more detailed discussion of power in economics and its absence in neoclassical theory. Very early on, Perroux lamented the relative absence of power, social classes, special interests in economic theory, and its reluctance to incorporate social hierarchy within its analysis. As Perroux claims, “Force, power and constraints are topics that are foreign to contemporary economics. Recent developments have not yet been able to integrate them” (ibid., p. 25; authors’ translation).

Although rooted in Marxist ideology yet contrary to Marx, Perroux’s (1961) analysis of power rests less on criticizing the capitalist economy than on discussing the effects of domination, which could apply just as well to socialist states as to capitalist markets. To this end, Perroux rejects the notion that power depends technically on the ownership of the means of capital. For him, it depends foremost on the position one holds within the hier-
archy or system of production, even though capitalism, which is defined by the ownership of the means of capital, necessarily implies a relationship between owners and nonowners (Byé and de Bernis 1987: 15).

For Perroux, economics is all about these relations; that is, the relations between those who dominate and those who are dominated. This dichotomy applies to all levels or spheres of social interactions: international, national, and even at the level of markets. At the international level, for instance, certain countries dominate trade; at the national level, firms dominate the fabric of industrial production. Within markets, there are always dominant firms that succeed in imposing their price. At the very least, industrial markets are characterized by oligopolies that try to exert their influence on the industry. Finally, at the level of the firm, management dominates workers and their salaries. For Byé and de Bernis, “The economic space of a country is a polarised space. Forces are exercised both within and outside of that space” (1987: 24; authors’ translation).

In Perroux’s view, this does not have to lead directly to a criticism of market economies, since such a criticism also applies to other types of markets. Rather, by starting with an analysis in which domination is the central theme, Perroux can concentrate on the complexity of economic interactions and analyze their unequal and dynamic nature. Such interactions are dynamic because, by emphasizing the dominant firms, the economist can discuss development or economic growth where these firms are central. In turn, these relationships are unequal because by emphasizing the asymmetrical nature of relationship, we can proceed to analyze the impact of social interactions, economic and social crises, and to study the importance of resolving conflict.

Nevertheless, Perroux’s approach does lead to a direct criticism of markets and individualist or atomistic behavior. Neoclassical economists perceive trade as a game of cooperation in which the preferences of two agents are confronted with one another. Trade is considered peaceful and obeys laws dictated by markets. This game determines prices and quantities, which in
turn determines equilibrium. However, what if the relationship is unequal? The transaction then must reveal its true nature: It becomes an exercise in power relations whereby a price or output can be imposed on another country, firm, or individual. It is no longer peaceful.

As an example, let us consider again trade between two agents. It would surely be coincidental if both agents possess equal power in entering negotiations. In other words, a strictly cooperative equilibrium remains rare. Indeed, according to Byé and Bernis,

Cooperative equilibria are a simple representation of competitive struggles \([\text{luttès-concours}]\). This argument is such a central element that advocates of general equilibrium models have developed a theory of distribution that excludes the conflict between profits and wages: the price of capital and labor are determined equally by the natural conditions of production. (1987: 479; authors’ translation)

More likely than not, the more a dominant agent succeeds in imposing conditions on trade, the more it will limit the other agent’s (the one who is dominated) preferences. Trade is by its very nature unequal. The dominant agent can either impose the conditions under which trade will take place or simply not enter into trade negotiations (Dupuys and Maris 1996: 5).

In these asymmetrical conditions, Dockès argues that the exercise of power, which is the conscious act of limiting someone’s freedom or choices, rests on a number of methods, more or less subtle, often giving, in fact, the impression that one’s choices are not constrained (1999: 25). In other words, it is not because an individual makes a rational decision that he is not subject or influenced by power (ibid., p. 27). Those who wield power can impose it in many (subtle) ways: through outright threats and economic sanctions or through some agreement that leads to a “double consensus”—which would benefit both parties—and a series of acts that would result in abdicating one’s freedom to another individual. The latter example, resting between one’s submission to violence and total agreement, represents in reality what Dockès calls “communicational power” (ibid., p. 45), which rests on numerous incentives, negotiations, or conviction whereby even the dominated
agent can see smaller gains. In this sense, “Market power can be interpreted as the positive side of economic dependence” (ibid., p. 45).

Let’s assume that purely cooperative exchanges can exist. Even under such conditions, an individual’s choices can always be constrained or limited. For instance, neither agent has the luxury of choosing not to trade or even to question the existence of the contract itself. This, in fact, amounts to a limitation of both agents’ freedom. This is a direct criticism of neoclassical theory: We cannot assume that cooperative exchanges lead to peaceful relationships between individuals. This is far too unrealistic. At no time is the market a peaceful trading place. Perroux’s contribution is to show that markets are in fact a place of “great violence.”

Post-Keynesians also describe a world dominated by asymmetrical positions and hierarchies. Yet, we believe that it is a better criticism of neoclassical theory and a better foundation for the development of power because it is rooted not only in the recognition of a hierarchy of agents but also in the fundamental belief that the world in which we live is fundamentally uncertain.

**Post-Keynesians, Power, and Uncertainty**

The notions of uncertainty and hierarchical relations within the production process are well-known and well-studied concepts in post-Keynesian literature. Yet until now, these two fundamental tenets have never been discussed in relation to a theory of power. Interestingly enough, post-Keynesian theory lends itself well to an analysis of the existence and exercise of power.

In post-Keynesian theory, the macroeconomy is divided among several macrogroups, each with specific relations with each other. For simplicity, let us consider three groups: money-creating banks and the central bank, which sets the rate of interest and generates money endogenously; firms that initiate the production process by borrowing credit from the banking system, which generates incomes and leads to a level of effective demand; and finally, workers and wage earners who sell their “labor power” in exchange for a wage. (We could obviously add the State, as well as “the rest of
the world.” See Pressman [2006–7] for a discussion on the role of the State and the exercise of power.)

From this analysis flow a number of specific relations. Indeed, firms depend on banks to access finance and credit with which to pay workers; workers in turn depend on firms for employment and income.

This hierarchy is a central theme of post-Keynesian theory. For post-Keynesians, the hierarchical structure is fundamental; it is the central theme of numerous papers about banks or firms. It emphasizes the asymmetry among agents and their relative standing in the specific hierarchy. Although post-Keynesians do not specifically address the various categories of agents—which are at the heart, however, of the monetary circuit approach—such an analysis is nevertheless implicit to their approach.

Post-Keynesians propose a model of production that integrates all agents; production is not simply a matter of output but involves workers, banks, laws, and so on. The functional division of agents—already present in Quesnay, Marx, and Keynes—revolves around three specific groups of agents and also around relations among them. Finance is performed by banks, firms assure the production of goods with the hiring of workers, and households spend. Moreover, given the analysis of the economic flows, the hierarchical relations among agents constitute the heart of the post-Keynesian analysis of the productive process. In fact, if every flow deserves specific study, a general discussion of the relations among these flows offers the possibility of capturing the dynamic nature of the economic system. These flows constitute a sequence of “economic events.”

In the post-Keynesian analysis, hierarchy (or hierarchical structure) refers to the distinction between the different functions of the agents and their interdependence and to the distinction between the monetary flows necessary for the productive process and their order in that process. At every stage of the production process, the circuit describes the monetary mechanisms, the relations among the agents, and their economic activities.

However, as we have already stated, the recognition of the asymmetry of positions among the different agents, which emphasizes
the power relationships, is not a new approach. Past economists were perfectly aware of this matter. The mercantilists, the physiocrats, and the classics have all integrated into their conception of the world the differences of status among agents. Without them, it would have been impossible to consider that an agent could have power over another. The truly original contribution of the post-Keynesian approach, we think, is to combine into a single analysis the necessary hierarchy of agents inherent to the production process and the prevalence of uncertainty characterizing the real world.

The Dynamics of Power: Uncertainty, Conventions, and Macroeconomics

One of the main objectives of post-Keynesian theory consists of showing the reality of the economic system. In the real world, perfectly competitive firms are certainly not the norm (if they exist at all), firms are not price takers, unions exist, and institutions play an important role. Post-Keynesians recognize these stylized facts. In this way, the post-Keynesian theory is not satisfied with a simple analysis of the market. According to Arestis, the post-Keynesian “method relies on moving from a set of ‘stylized facts’ that indicates the existence of a phenomenon that necessitates ‘deeper’ explanation, to a theory to analyze the underlying relations, structures, conditions and mechanisms which are responsible for the given phenomenon” (1996: 115).

The emphasis on uncertainty—regrettably neglected by Perroux—carries a number of implications for economic analysis. Not only does it allow us to describe the complex world of agents’ expectations, but it also allows us to explain the existence of conventions and the crises they can generate. It is, in fact, the very discussion about uncertainty, conventions, and crises that allows us to introduce within post-Keynesian theory the importance of power relationships and their emergence.

The system described by post-Keynesians evolves through time: This is a result of the realization that it takes time for the variables to play out. As Davidson observes,
The production of goods takes time; the consumption of capital goods and of durable goods takes time. These production and consumption processes are, by their very nature, irreversible. Real time is therefore an asymmetrical variable, meaning, among other things, that although we may know the past, we cannot know the future. (1985: 260–1)

Because production takes time, unforeseeable events can occur that can alter the course of events. In particular, time, by definition, leads to distortions in the flow of information. Although it is easy to analyze the past, the future is uncertain, leading all economic agents to make economic predictions as best as they can. Agents’ ability to make predictions is limited to human capacity to deal with a certain level of information of highly complex possibilities.

In this sense, all economic variables must be understood within an environment of radical uncertainty or nonergodicity. Similarly, institutions, relationships, firms, households, and other agents all live in this same environment. The objective of all agents is to try to have control over this environment of pure uncertainty as a tool to reach their other objectives. For instance, whether firms maximize their profits or pursue “satisfying” profits, growth of sales, or market shares—in fact, irrespective of what their precise goal is—they try to reach it within an environment of uncertainty. This means that to achieve their goals, they must somehow be able to control their immediate environment. For instance, they try to control the price of the inputs of production, such as wages, and seek to control the distribution of their product, as well as advertising. The same logic applies to all other agents. The unknown future presents many obstacles in the realization of agents’ objectives. Workers try to control wage increases and in fact resort to creating institutions (unions) to give themselves more clout in the collective agreement process. Banks face considerable uncertainty regarding future levels of effective demand and thus uncertainty regarding the ability of firms to reimburse their debt. As a result, they may cut their lending if uncertainty and pessimism about the future level of effective demand grows (see Rochon 2006).

In an uncertain world, therefore, each social group may want to try to exert more power over their immediate environment. Uncer-
tainty and the unknown level of effective demand in the future become the very sources of power in economic analysis. All agents in the social and economic hierarchy want to minimize this uncertainty by amassing information, although this ability is often limited by the availability and quality of this information. According to Arestis, individuals “are not omniscient and able to acquire information, but their capacity to do so is limited. . . . Market forces cannot deal with the unknowability and unpredictability of the future, and therefore can only disseminate incomplete, and even misleading, information” (1996: 116–17). Having more information than others in a typical dominant–dominated relationship can indeed lead to greater power over the dominated group, although it does not eliminate uncertainty. Institutions are often created with the purpose of amassing information for the benefit of those who own or control the institution.

As such, radical uncertainty constitutes not only a privileged tool to understand the expectations of economic agents (in particular, firms and households) but also allows us to understand power relationships and how they emerge. It allows us to see the relations among uncertainty, institutions, and power.

The crucial question is the following: If agents want to control their environment—given that they exist in a world in which the realization of their objective depends on the actions, decisions, and behavior of other agents—how can they best control their environment and impose their will on others?

Agents’ expectations and predictions are taken within a framework of conventions, which aims to reduce the effect of uncertainty on agents (see Figure 1). The absence of knowledge about future events leads post-Keynesians to believe not in the rational agent but rather in the “conventional” agent (Barrère 1990). In fact, post-Keynesians defend the notion that “it is the conventional behavior that governs our expectations and forecasts. This is different than the rational behavior assumed by the real theory, which operates within a world of stability or probabilities” (ibid., 51).

Conventions are a normal reaction to uncertainty and offer agents a stable frame of reference. The next step is to legitimize these
conventions by transforming them into institutions (e.g., contracts). It is not surprising to claim that institutions are born from conventions: Laws are often enacted based on practice and customs, as history tells us. Arestis argues precisely that there “are two institutions distinctly important to our analysis: the large corporation and the trade union. . . . The large corporation, and more importantly the recognition of its market power and ‘stylised fact’ that firms are price-setters and quantity-takers, are highlighted in post-Keynesian economic analysis” (1996: 118).

Even if Arestis (1996) minimizes the number of institutions studied by post-Keynesians, he nonetheless allows us to see the relation between conventions and institutions, which can then lead us into a discussion about the existence and exercise of power. The causality is that uncertainty leads to the emergence of conventions and institutions, whose role is to minimize uncertainty and exert power.

The Analysis of Emergence of Power

So what of power? The legal context leaves a priori little place for consideration of power, because it is an expression of the collective and the acceptance of an authority (Dupuys and Maris 1996). If we can call into question the legitimacy of existing power—is the law a product of a democratic process or the expression of the will of pressure groups?—the legislature does not allow for the development of new powers because it determines the types of relations between different economic agents. As such, firms do not possess the means to exploit their employees to their own advantage without exposing themselves to employees’ right to work relative to hours worked, minimum wages, and so on. Thus firms
must either break the law or demand that the law be changed to achieve their goals.

In reality, power begins to express itself further upstream; at the moment that conventions appear. Born of uncertainty, they leave the field open to any appropriation of power because agents are in search of authority, formal or informal, to make their economic calculations in the best possible conditions. It only makes the appropriation of power that much more efficient. The agent, possessing the means to impose its will, seizes this opportunity to defend its interests, having not faced any legal barriers. There is no want of examples, and it suffices to examine periods of great uncertainty to witness the emergence of new powers.

Presently, with the growing effects of globalization, firms find themselves invested with new powers in the absence of substantive jurisdiction in matters of production at the global level. Although the embryo of an international exchange legal framework is developing, major questions regarding production remain. It is now commonplace—in fact conventional—that firms use relocation to lower production costs and, as leverage, to put pressure on their countries of origin.

Disposing of this new power, companies are at present more than ever in a position to impose their will. For some, largely decried like the International Monetary Fund, they represent a means of operations for the State, conventions more or less satisfactory on a global scale yet still in search of true legitimacy and a legislated framework.

However, the concept of radical uncertainty allows the analysis to go even further. Far from being a simple explanation of conventions and power relations, uncertainty enables us to examine from this point of view how these periods of crisis are particularly well suited to the emergence of novel powers and the production of great economic instability.

**Power, Uncertainty, and Crisis**

Periods of crisis are characterized by great uncertainty and the emergence of new powers. Post-Keynesian analysis has provided us with new concepts capable of shedding light on the relations...
among uncertainty, institutions, the insufficiency of effective demand, and the exercise of power.

Post-Keynesians explain effectively that institutions must intervene to limit the uncertainty usually felt by agents. As Davidson explains, “government should develop economic institutions which attempt to reduce uncertainties by limiting the possible consequences of private actions to those that are compatible with full employment and reasonable price stability” (1996: 66). Thus, the authorities know when they can intervene over the temporal horizon of their expectations to reduce uncertainty. However, periods of crisis are characterized by strong uncertainty, which leads to the thinking that the means of uncertainty reduction are not in place or don’t work anymore (see Figure 2).

First of all, this is not without consequence. If uncertainty grows, one must expect a decrease in effective demand because when the “agents’” fear of an uncertain future increases their aggregate demand for “waiting” (even in the long run), agents will divert their earned income claims from the purchase of the current product of industry to demanding additional liquidity. Consequently, effective demand for labor in the private sector declines (Davidson 1996: 63). Thus we have two scenarios (see Figure 2): Either a simple increase in uncertainty results in insufficient effective demand or an existing crisis is self-maintained. In these cases, nothing has been attempted or nothing works to relieve uncertainty.

Then we can question the explanations of the appearance of increased uncertainty because “this distinction between ‘normal’ and ‘abnormal’ periods will lead Keynes to new development as
soon as he recognizes that different periods have different characteristics. . . . ‘Normal periods’ are characterized by uncertainties; their world is one of uncertainty” (de Bernis 1995: 385; authors’ translation). Putting aside the situation in which a crisis already exists (see Figure 2; second arrow), thus naturally creating uncertainty, let us examine the case in which uncertainty seems to grow with no apparent economic explanation (see Figure 2, first arrow). With growth an unknown element, various social classes try to appropriate a bigger share of income. Specifically, how will growth in the future affect the ability of workers to secure higher wages? How will it affect the income-generating process, retained earnings, and corporate profits of the firms? If rentiers are included, what will be the future levels of interest rates?

Indeed, the rate of interest is of paramount importance. As an income distributive variable (Lavoie 1992; Rochon 1999; Rogers 1989), power relationships are built within the rate of interest itself. As the rate of interest increases, income is necessarily transferred from workers and capitalists to rentiers (with consequences on economic growth given differential propensities to consume). In a monetary economy, the role that the rate of interest plays in power relationships is of particular interest.

In a typical endogenous money environment, there is a specific hierarchy present in the production process. Firms need to borrow credit from banks and must hire labor. Because production necessarily implies debt, firms must be able to reimburse their banks. They therefore must remain financially sound and credit-worthy as far as banks are concerned. Indeed, endogenous money is synonymous with the creation and destruction of debt.

However, if firms need to remain financially sound, they must be able to generate sufficient revenues. If future levels of effective demand are not known—indeed if uncertainty is prevalent—then firms will want to exert as much control over their environment to guarantee their survival (i.e., the repayment of debt and the continued support of the banking system). In this sense, power is an important element of a firm’s survival: It will seek to lower wages, control costs, and impose a higher mark-up, among other things. Because of this uncertainty, firms need some reassurance that they
maintain control over their environment. This is essential for their survival.

It is perhaps relevant to quote Lavoie once again: “The firm wants power over its suppliers of materials, over its customers, over the government, over the kind of technology to be put in use. . . . In a world without uncertainty, the notion of power dissolves and loses much of its importance” (1992: 99–100).

Post-Keynesians show that conventions and institutions are adopted to reduce this feeling. Why then do they cease to operate after a certain time? One can suppose, as does de Bernis that “these forces can never succeed in ensuring this effectiveness in any permanent way; there necessarily comes a time when these procedures become ineffective, the various national economies are once again thrown into uncertainty carrying each time new outcomes” (1995: 389).

However, it is precisely this institutional vacancy that allows for the appearance of new powers. If conventions and institutions no longer can reduce uncertainty, agents will turn to new conventions to control uncertainty. Consider the present: There is no doubt it is a time of great uncertainty. It is increasing and relates as well to employment, new technologies, and the persistence of national crises. However, the modes of intervention that we have no longer seem relevant. The authority of the states is called into question as much on the national level as on the international level, and the national governments have great difficulty in limiting the effects of globalization.

Conclusion

The purpose of this paper was to develop a post-Keynesian theory of power based on the existence of uncertainty. As we have argued, although many heterodox approaches explain the exercise of power, none really address its existence. Based on the work of post-Keynesians, Davidson and Lavoie in particular, we conclude that power cannot exist in a nonergodic world, which explains in part why neoclassical theory cannot incorporate power within its theoretical structure, except by introducing some “imperfections.”
The presence of uncertainty muddies the waters and makes the future unknown and unknowable. As a result, social groups will want to maximize their gains. As such, institutions are seen as a natural development in light of uncertainty, thereby becoming instruments of power benefiting those who can control them.

Notes

1. In fact, a quick perusal of a great many of the mainstream textbooks, at many levels, reveals that the concept is virtually absent. Irrespective of the level, the main textbooks, from Blanchard to Dornbusch, Hall and Taylor, Mankiw, Romer, and Samuelson, to name but a few, all are conspicuously silent on power. This suggests one of two things: Either economists generally do not believe that the notion of power is of any interest to economists, or they believe that power simply does not exist.

2. According to Max Weber, power is the “probability that an actor in a social relationship will be in a position to carry out his own will despite resistance, regardless of the basis on which this probability rests” (1978: 53).

3. The concept of losses is closely related to the notions of violence and coercion. As such, pure coercion assumes the existence of net losses whereas market power is synonymous with fewer gains.

4. Anticipation of firms $\Rightarrow$ production plans $\Rightarrow$ demand for banking advances $\Rightarrow$ credits $\Rightarrow$ monetary flows $\Rightarrow$ flow of equivalent incomes $\Rightarrow$ household portfolio decisions $\Rightarrow$ residual amounts of currency (Goux 1996: 83).

5. We should note that the expectations of agents are based more on mere instinct and “animal spirits” than on logic or reason.

References


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