

Economy and Democracy
A Theory of Finance *à la* A. De Viti De Marco*

by
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*A Paper to be read at the XIII Conference on input-output techniques, Macerata. I am particularly honoured to read this paper in Macerata, where young A. De Viti De Marco once taught political economy.

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1. In the usual modern industrial countries, the contribution of the political or governmental sector is substantial. Sixty to eighty percent of the GNP of a country is produced by its industrial sector, while the remaining forty to twenty percent by its government sector. Usually the economics deals with the former only, but the latter is the subject of financial economics. These figures are different from country to country and depend on the stages of development of the country.

In the case of the private sector economy individuals' and firms' activities are structurally stable; individuals maximize their own utilities, and the firms their profits. On the other hand, in the case of the public economy, the character of the decision maker, the government, changed rapidly and drastically in the nineteenth and twentieth centuries, so that we cannot derive a stable and persistent theory which explains the government's behaviour on the basis of which the general theory of public finance is constructed. We can at most review and examine particular cases of economic policy of the government.

At the end of the eighteenth century three of the present day advanced industrial countries, namely Britain, France and the USA, had already constituted an independent unified country, but the other three, Italy, Japan and Germany, had been broken up into many feudal domains. In order to form a powerful industrial country they had first to be unified as was actually done in 1861, 1868 and 1871, respectively. The former three were called advanced capitalist countries, whilst the latter three were often referred to as younger capitalist countries.

Among these, Japan was rather exceptional; she was sometimes categorised as a country of 'centralised' feudalism, because one of the domains surpassed the others. Even so the government of that domain was patrimonial; no element of democracy was contained. The government was financed so as to maximise the satisfaction of the tycoon family. Similar patriarchalism and patrimonialism prevailed in local domains. Therefore, the tycoon Tokugawa's government, which was taken as the then central government of Japan by the foreign powers, was feeble in handling international matters. It was pulled down by the other major domains collectively. This resulted in the unification of the domains in Japan, i.e. the so-called Meiji Restoration or the Meiji Revolution.

The three countries that had been unified more or less simultaneously became very aggressive and imperialistic in order to recover disadvantages due to their belated starts. Japan won the 1894-95 war against China and the 1904-5 war against Russia and annexed Korea in 1910. In 1882 an alliance was formed among Germany, Austria and Italy. In spite of this, Italy fought against Germany and Austria in World War I in 1914-18. After the war Mussolini became more and more powerful and swung to the right. In Germany Hitler took power in 1933. During these years Japan invaded Siberia, then the north-eastern part of China (Manchuria) and finally mainland China. These three militaristic, totalitarian powers concluded a military pact in 1940. Their governments entirely changed their character as they degenerated into the ones for total war. On both sides of the warring powers miseries were created and accumulated in the working and farming classes, as they were major sources of military recruitment. Welfare considerations of the working class became a serious matter after World War I and created socialist movements in industrial countries. When it was realised that World War II would soon be over with their victory, the British people chose Attlee of the Labour Party rather than the war hero Churchill as the Prime Minister. Thus the age of military and police states ended, so that the structure and spirit of the governments were revolutionarily changed.

After the War the governments of most nations were democratised at least on the surface of the principle or literal expression. The meaning of democracy is, however, different from country to country. Even between the UK and USA, it is not the same. Their political structures widely differ from each other; the procedure to decide on the Prime Minister of the UK does not bear the slightest resemblance to the election of the President of the USA. In the following, I take the UK as the model country of democracy and discuss how the financial policy of the nation is decided, implemented and revised if necessary.

2. The main subject of the manifesto that a major political party declares at the time of general election is the financial policy that it would implement in the case of it being able to command a majority in the general election. If it cannot commit itself to that policy, it will be severely criticised and may be highly likely to lose the next election. The manifesto should be consistent but should not be one-sided, because if so, the party would not be supported by those persons who are particularly interested in certain kinds of political and economic

problems. Concentrating its attention upon a certain limited number of problems, the manifesto of the party must be well balanced. This means that it does not describe the simple, unconditional optimum programme of public finance. It is a mixture of allegation and compromise, so that an approach of assessing political possibilities in terms of a well behaved, consistent, objective function cannot be adopted even in the case of the shortest period of analysis. No major party has a straightforward programme of policies. It always has a set of means, which pacifies those being disaffected by the government policies.

It is usual, therefore, during the period of office, that the majority party led by the Prime Minister will modify or soften the policies by mixing them with a means for soothing dissatisfied people by taking into consideration what they have learnt from experience in the previous years.

Nevertheless, the principal part of the manifesto that the party promised at the time of general election will be accomplished; if the majority of the people appreciate it, the party in office will be re-elected. In most cases, there will be one substantial change in the direction of politics that will be carried out by the succeeding government. Where the present government party is defeated in election, a different party comes into power, and its manifesto will be implemented subject to minor modifications and amendments. However, in comparison with the political course taken by the previous government, there will be observed a substantial change in the course that the new government will adopt. If the change is big enough we may say that there is a political innovation. Otherwise it is only a shift in stance, a mere reconstruction of an old building.

The aim and spirit of nation-states fundamentally changed in 1945. It was no more the age of military states. Each major country had to start the work of transformation of the previous military-industrial structure into one for a welfare state. As both Conservative and Labour Parties had worked in the framework of a military state in the pre-1945 years, they had to propose manifestos which accorded to the welfare state line in successive general elections. Of course, the movement of welfarism was initiated by the Labour Party, but it was succeeded by the Conservative Party. Excesses of the movement that had been made by the Labour Party were corrected by the succeeding Conservative. Even the rightist age of Margaret Thatcher would be appreciated, as it should be, as a right and proper correction of

the excessive left-wing way of thinking of the Labour Party. When she went too far, she was replaced. In this sense the democracy of the British type worked in the latter half of the twentieth century. The state policy, i.e. the financial policy of the state, staggered but remained the chief pilot of the history of Britain.

At the time of general election, the main policies of a party contained in its manifesto are made clear to the public. The most successful one in the recent history of Britain is the one for establishing the Welfare State. It is an ambitious, comprehensive and long-standing programme that was started by the Liberal Party at the beginning of the twentieth century and was kept alive under the war time restriction until 1945 by the Labour Party. It consisted of a number of large important projects which came into bloom when Labour led by Attlee took power. The establishment of the National Health Service (NHS), introduction of state pensions, improvement to education, and nationalization of a number of industries may be regarded as major components of the whole Welfare State programme.

As it was so enthusiastically supported by the people, even the Conservative Party too had to propose a manifesto which was in line with promoting the idea of the Welfare State. At last, in 1970, a completely different topic entered the arena of British politics, that is whether Britain should join the EC or its development such as EU. Also, it started to be questioned whether the scale and quality of the Welfare State programme that successive British governments had aimed to accomplish exceeded the capability of the nation or not. Then politicians began to consider that some degree of privatisation of sectors of the Welfare State, so far established, would be a reasonable point for consideration at the time of general election; but this does not necessarily mean a U-turn from the Welfare programme. It would merely mean a correction or adjustment. It only meant that a better and more efficient way of achievement was groped for. In the most recent 1997 general election when Blair came into power, he confirmed that under his New Labour the Welfare programme would be kept healthy and the extreme leftwing movement would not be allowed. He, in addition to this, promised to the residents in Scotland and Wales some kind of devolution, though its detailed particulars were not clear at that time.

3. It is well known that economic innovations are in the hand of businessmen. The ideas are formed individually and secretly. They are implemented and made workable through markets, where the competition is made among individuals and firms. In the same way ideas

of political innovations are discussed in secret by the top members of the party and are made public at the time of a general election. As has been mentioned already, the economy of a nation state consists of two sections: private and governmental. The members of the former, individuals and firms, are connected with each other through markets where they compete with each other. On the other hand, the members of the latter engage in competition throughout the campaign period of the general election. There are big differences between the fates of the winner and defeated. As long as it remains in power, the party behaves, more or less, as a monopolist in political affairs; those plans which were proposed in its manifesto would be carried into effect. The opposition parties would offer resistance to the proposals of the government and try to mutilate the bills, but power would be in general in the hand of the government until the time of the next general election. Democracy according to the parliamentary system prevails in this way, so that it is consistent with a short-run dictatorship that is obvious in the citizen's eyes.

The markets for the private sectors are opened regularly every day, whilst the market for the public sector, that is the general election for selecting the party in power, is available only intermittently once in five (or four) years. In the Western democratic countries the competitive mechanism works more or less in this manner. In both sectors economic or political innovations play the most important roles. They would broadly change directions of advancement of economic and political sectors, respectively. They have been designed secretly before they are presented in the market or the campaign for election. Once they have been revealed, they become the people's open targets for examination and dispute.

As Schumpeter has written about economic innovations, those which have changed the face of the economic world are neither savings nor increases in the available quantity of labour but are identifiable by the fact that entrepreneurs have been able to switch to different method of utilisation of resources.¹ Similarly, a political innovation does not need extra resources; but yet it can make a thorough change in the course that the nation will take. It is, often, presented together with detailed minor programmes which support and supplement the principal idea of the innovation. It can have an enormous effect upon the private sectors as the effective demand of the public sector for the produce of the private sectors and the effective

¹ J.A.Schumpeter, The Theory of Economic Development, Harvard University Press, 1951, p.68.

supply of the produce of the public sector greatly changes so as to back up and realise the political innovation.

4. The philosophy of Welfare Economics is not necessarily consistent with the above view of historical development of politics of the nation state. Each party in power has not completely executed the whole programme that it promised in the last election manifesto, at the time of the next general election. If it proposes the remaining part of the same programme again, it is highly probable that it will be defeated by one of the opposition parties, so that an entirely new item is usually introduced by the present party in power. Similar revisions or alteration will be made by other parties too. Thus the policies actually adopted do stagger at the time of each election. They are not results of some kind of optimisation of an objective function but no more than results of a sequence of brave choices. There is no exact marine chart useful for travelling the political world of innovations. Through the progress of time, the character of activities of the nation state and their aim and sphere of influence are rapidly changing from time to time. Concentrating our attention upon the analysis of the private sector we have obtained a number of general equilibrium theoretical conclusions; but they all have to be subject to some kind of amendment if we take into account the everlasting movement of the political sector.

UK is not the only country which can claim after the War as a would-be Welfare State. Sweden and Norway belong to the same category, but they are very small. In terms of the number of inhabitants, Sweden is comparable to the Greater London area, and either of Norway and Denmark is half of it. In comparing UK with other less developed Welfare States such as USA, France, West Germany, Japan, etc. we must begin with finding and providing a measure in terms of which the performance of relevant countries is examined. The real value of the GNP per capita, however, is taken, as usual, as the measure of comparison. Then we find that in terms of the achieved level of welfare UK is higher than other industrial countries, USA, France and others, whereas in terms of the real GNP per capita UK is very low in the list of the countries compared. Especially so in view of the fact that the distribution of income is more even in the Welfare States than in the usual industrial countries, and it is logically found that British people in the position of highly paid jobs are poorly paid as compared with the corresponding persons in the industrial countries with less welfare consideration, so that they feel envy of them; Britain has thus experienced a period of

brain or ability drain that has to be counted as a part of the cost that must be accepted for the establishment of the Welfare State.

It is evident that an expansion of the technological production set of the private industrial sectors gives rise to an increase in the level of welfare that the government can achieve. It is thus seen that the technological innovations promote political innovations. Then it would highly probably happen as has been seen above that the Welfare State will lose industrial, managerial and academic experts to industrial competitors. This would create a check on the welfare movement: too much welfare would endanger the country. This is particularly more strongly believed by those persons who consider that the workers do not work hard if they are provided with a high level of welfare without making any payment. Then a retreat from the work of constructing a perfect welfare state, such as Mrs. Thatcher's privatisation policy, has a reason for it. Neither too much or too little welfare is acceptable, so that there must be an optimum between them. But, as has been seen above, this optimum is not decided by maximising some kind of Welfare function, but by the opportunism that the political innovations make possible to the parties. As long as party leaders believe that they will get a greater number of votes if they pursue welfare policies more densely, the movement towards a higher grade of Welfare State would continue further.

Let us now ask why the political innovation which was intended to establish a Welfare State became feasible at the critical point of time when World War II was considered likely to cease soon. We may point out at least a few items to be taken into consideration. First, after the War the government expenditure would be expected to decrease significantly; then a depression that would be greater than the Great Depression in the thirties would follow. If the government could do nothing to avoid that sort of catastrophe, the people would have to repeat the entire history that we had after World War I: severe confrontations of workers against capitalists would develop into rightwing movements of Fascist or Nazism type. Thus we should not decrease the level of the government's effective demand at all; this was the first principle of the post-war politics. Secondly, because of the long time efforts of Fabians and others, familiar to the British people had been the importance of philanthropic works, the general education of the working class, improvement of sanitary facilities and so on. They were already convinced by the view that unemployment and poverty did not result mainly from the laziness of the people, but the responsibility for them, like that for the defence of

the nation, was easily taken as the duty of the government. That is to say, armaments and welfare programmes were good substitutes at the time of 1945. There is no objection from the people to increased welfare as a substitute for armaments.

If it is accepted that it is the duty of the government to keep the people's welfare at an appropriate level in the same way as it assures them their safety satisfactorily, then the prime condition for a welfare state is that the people are given medical care freely whenever they need.² This means that the philosophy of the British national health service was entirely different, at the point of time of its start, from the motive of establishment of health insurance companies in usual capitalist countries. In the same way, it is regarded as the duty of the state to provide a reasonable level of living to senior citizens, so that it is entirely different in spirit from a company's annuity scheme. These British welfare arrangements are based on the revolutionary change of the people's view of the state, and these political innovations became feasible because the people of the country supported that party which was going to carry out the programmes based on the new view of the state. In this way, without having disturbed the level of taxation greatly, the government could let their entirely new policy set sail safely. Its set of policy possibilities is not only enlarged but also changed into in an entirely new direction. It obtained a new richly cultivatable world. It must of course be added that this achievement could be realised by getting the support of the people's leftist mentality which had culminated in the period of 1920s and 1930s.

Also, it is a very great task to abolish entirely or partly slums in urban areas. Not only were houses in shortage there, but also had become very old, so that they lacked various amenities that recently built houses of more or less similar quality must be equipped with. After World War I local self-governing bodies were put under an obligation to provide houses for workers. They increased the stock of houses at the pace of 50,000 a year in the period 1919-1939. Of course, this programme was resumed after World War II. Houses were produced by local self-governing bodies by 150,000 a year in the post war five years, 1945-1950. This may be interpreted as the fact that the government considered the supply of the minimum level of housing to poor workers its duty in the same way as having taken the NHS as the duty of the government.

However, it was a very difficult task, because the demand for houses in the urban area increased rapidly. Confronted with this huge shortage of houses, the government dealt with it by creating entirely new towns. If they are built in a neighbourhood of a city, it is no more than an idea to enlarge the city itself. If they are built in remote places isolated from others, then each new town must be self-contained. It must have an ability to create enough jobs which support the entire population of the town, so that no new town can just be residential. It must be industrial and attract various kinds of individuals. We may then say that the 'new town' programme is no longer a Welfare programme but a comprehensive programme of the socialist nature. It is not surprising to see that the new town movement once having been very popular in the post World War II period eventually lost its popularity and declined.

5. Although the philosophy of the Welfare State has to be distinguishable from the philosophy of socialism, it is true that they were actually related to each other. Railway companies which had been independent except for the two World War periods were nationalised in 1947 by the same Attlee government which established the NHS. The same government nationalised a number of major industries such as the Bank of England, civil aviation business, coal mining, submarine cables, wireless telegraphy, transportation, electricity, gas and steel. After Attlee, four conservative governments successively took the power; there was no major nationalisation during that period, but as soon as the power was switched from the Conservative to the Labour, the steel industry that had been denationalised by Churchill was re-nationalised by Wilson. In this way the period of nationalisation, denationalisation, re-nationalisation, and so on emerged in Britain. This yo-yo period continued until Mrs. Thatcher finally took power. During the period of her rule, the philosophy of Welfare State as well as that of socialism declined. It would have been difficult for Blair to re-take up power if he did not reform his party as the 'New' Labour clearly distinguished from the 'Old' Labour. Though in the defeated Conservative Party the Thatcherite members seem to be still powerful, the backing of public opinion upon them is weak. Blair may enjoy a politically favourable period which will be expected to continue for a fairly long period of time. The yo-yo will stop in this way; then we have in Britain a mixed economy consisting of private industrial sectors which are capitalistic and public sectors which are mildly socialistic.

² This is the same as the way of Adam Smith having written about military services.

It is natural that the same attitude which the society had taken on health and health care of its members was also adopted concerning their housing at the minimum level bearable by human beings. In UK, before 1914, the local governments and municipal corporations began to provide houses at low rates; this was accelerated during World War I considerably. The same thing was repeated in World War II, with the outcome of a number of new towns projected and completed by public corporations formed for the purpose of development of new towns. This may be regarded as a conspicuous link in the socialist movement that was raised after 1945. It is needless to mention that economic activities of the state were enhanced in parallel; coal, electricity, international communication, railway, bus and various truck transportation, the Bank of England and others were nationalised after 1945. In addition to these, education was modernised in 1944, in order for the people to regard education, like medical care, as a basic human right which the society should recognise. Since the people were not satisfied with the schools, modern school and comprehensive one, that the education reform had introduced, it is true that the problem of education as a basic human right for children has not been settled yet. It is nevertheless true that this humanistic-socialistic ethos has enlarged the scale of the state significantly.

Independently from this movement, it is observed that industries were nationalised in a number of countries as understandable consequences of World War I. Obviously the state imposed heavy taxes upon the people, during the war period, for the purpose of accomplishing the war. The taxes thus collected had been poured on munitions industries mainly, but the demand for their products of course became very insignificant after the war. Other industries were starved throughout the war period. It was found that all industries were left in a disastrous plight. To reconstruct industries the government had to help wrecked companies and factories by pouring enough money to clear their deficit. For that purpose the fascist government of Italy established an institute for the reconstruction of industries (IRI), which became the government's arm for nationalisation of industries. In Japan, during the war period, nationalisation was not the main weapon for controlling industries. The government could have manipulated the economy by allocating the labour force and raw materials and indicating the target for each output.

In any case we have to say that for various reasons stated above the central and local governments have become larger and larger and have been more and more involved in manipulating private industries, in addition to operating public enterprises. We may say that

in the last quarter of the 20th century about 30% of the national income of an advanced country is directly or indirectly produced by the government and public sectors.³ This means that it is now most important for economists to investigate how decisions are made for them. It is evident that their decisions are not entirely economic but mainly political.

6. Then, how is a government's decision made in the modern state? The answer is, it is, or at least should be, made democratically. Although the time at which a state has become democratic differs greatly from one to another, most countries now claim themselves to be 'democratic'. But their definitions are different from one another. A 'democratic' country may be 'undemocratic' according to the definition of some other country. In the following I assume that the state is democratic in the British sense.

The United Kingdom has traditionally three major political parties, Labour, Conservative and Liberal Democrat. In terms of the numbers of supporters revealed in opinion polls, the most popular party is usually supported by 42 - 45% of the electorate, the second party by 37 - 41% and the third by 17 - 23%, the rest being shared by minor local parties. If the first party actually obtains 44 or 45% of the votes in the general election, while the second party only 37 or 38, it is almost certain that the former gains an absolute majority in terms of the members of Parliament. Where the first party only gets 42 or 43% of the votes and the second 40 or 41%, the result in terms of elected members of Parliament is very close between the first and second parties, so that there is a possibility of a coalition cabinet; but it is a very rare case except for a transition period when the third party is rising up rapidly. In this sense we may say that the British political construction has been very stable, in spite of the changeover when the party which has been in power is pulled down by another one, as is often observed when a general election has taken place.

This three party system would exist in a nation where there are three categories of people, (a) conservative, (b) progressive, and (c) free and unbiased. It is necessary for its

³ The figure of 30% is merely a rough guess, because all the available input-output tables are described in terms of total sectoral outputs and inputs including both private and public outputs and inputs. Unless we make some additional assumptions, it is impossible to spell out how much of increased induced demand for a commodity remains within public sectors and how much of it flows out to private industrial sectors. . On the basis of Hicks', The Social Framework, Oxford University Press, Table VIII of the second and fourth edition, respectively, the proportions of the disposable income of the central and local governments to the total disposable income are

prevalence that the people of the same category are not concerned with the difference in the degree of thickness of the characteristic. For example, the conservative may be subdivided into three subgroups, ultra-conservative, moderate, and progressive conservative. If each of these insists and sticks to its essentiality, it is impossible to have a comprehensive conservative party that is supported by all types of conservative individuals. Similarly, generous and tolerant attitudes must prevail among progressive people. Liberals also must not be too rigorous and insistent. Thus the parties are formed on the basis of broad ideologies.

Detailed policies of the party are formed without consulting with ordinary members of the party as well as the general populace. Nevertheless, each party commits itself to its policies at the time of general election by publishing its manifesto, that is the document tying up the policies actually adopted to those described therein. Voters choose their favourite candidate mainly on the basis of information they have gathered from the party manifestos. The majority party forms the government that is implemented to carry out the policies more or less along the line described by its manifesto. The policies are discussed in the parliament, but there is no difficulty for them to be approved because they are proposed by the majority party. Of course, they are sometimes revised or rejected. It is extremely rare that a referendum is made in order to decide the matter. Thus, in most cases the government's decisions get through Parliament, without consulting the people. As far as this aspect of policy implementation is concerned, there is not much difference between dictatorial and 'democratic' governments.

The party that has been recognised as the majority cannot remain so for more than a period specified by the election law (five years in the case of Britain). At the second time of election, not only other parties but the ruling party too publish their election manifestos and the electors examine the government's performance during its period of office (say five years in the past), in addition to making comparison of the contents of parties' present manifestos with each other. This election is of course democratic but the implementation of policies is 'dictatorial' in the sense that they are carried out without further consultation with the electorate. During those years the majority party has been trusted by its supporters, so that the government could carry out its own policies. When it finds them to have been excessive,

obtained to be 21% in 1949 and 26% in 1969. But these do not include the repercussion effects upon the activities of the public industries.

adjustments and readjustments will be made in following years. More significant alterations are introduced in the manifesto for the next election. Thus the behaviours of the political and public sectors are intrinsically dynamic.

Nevertheless, economists usually neglect the government and public sectors or regard them as given bodies or entities that are not explained endogenously within the system; it is then seen that the economy will settle at some, static or dynamic, state of equilibrium, provided that there prevails perfect competition between any pair of members of the private sectors as it is so in the state of Hicks' regularly progressive economy.⁴ At the equilibrium point we observe that neither individual nor firm can improve his or its position without causing at least one of the others to suffer. We must remember, however, that the economy does not settle at this point of equilibrium (temporary equilibrium) ultimately; the government sectors react to this performance of the economy and alters either their decisions, or a different party may come into power. Therefore, very different behaviour of the government obtains. In this way the economy will move out from the previous equilibrium to a new one. As a result of this movement a number of persons may benefit, whereas others will lose. This means that once the self-adjustment of the government sectors unseparably related with the formula of democratically choosing the government by election is recognised, then we are led to the view that neither static nor dynamic economic equilibrium analysis, with given government sectors' demands for goods, is suitable to explain how the economy of a modern nation-state works through time. The whole economy is totally intrinsically dynamic.

We all have been taught by J.A.Schumpeter that it is the role of entrepreneurs of the private sectors to carry out innovations or what he calls new combinations. He has classified innovations into five categories, among which the following three are important: (1) producing a new quality or a new kind of a good, (2) introducing a new method of production and (3) carrying out of a new organisation of production.⁵ These are for private sectors. Similarly, for the government sectors too, the concept of innovation plays a very important role. The establishment of national health services that I have discussed above is nothing other than a great innovation. The idea of new town construction is also epoch-making and

⁴ J.R. Hicks, A Contribution to the Theory of Trade Cycle, 1950, p.86.

⁵ J.A. Schumpeter, The Theory of Economic Development, 1951, Harvard University Press, p.66.

highly innovative. As new towns have to be provided with highly advanced and useful infrastructures, in order to produce them the corporation for development of new towns must have an ability to develop industrial innovations like those of (1), (2) and (3) above. Thus, political and industrial innovations are key concepts which are crucial for explaining the development of government and public sectors. Unless a party has an ability to devise new political combinations, it is almost impossible for it to come into power.

7. In this section I review how modern economic theorists have dealt with the economic role of the government. Among economists, these are agreements in viewing the economic framework of modern states. They are all consistent with formulating a comprehensive model consisting of two compartments: (1) private compartment and (2) governmental and public. Walras, for example, assumes in his work of general equilibrium⁶ throughout, that the government is not usually involved in economic activities, though he is concerned with discussing the monopoly of railways, apart from general discussions of economic policies and social economic problems. We must say, as far as his theoretical works are concerned, the government is an absent, or neutral spectator. It may decide its verdict upon what has happened in the private sectors but is never involved positively in economic activities there. After him, a strong tradition has emerged among economic theorists: theory is purely economic in the sense that the government and public sectors are entirely absent. Then political value judgements are made on the economic achievements obtained in such a pure, imaginary world. Most famous examples are Kenneth Arrow's works on extension of theorems of classical welfare economics.⁷

If we take into account the fact that around the central government, local government and various public sectors are formed, we can no longer take for granted the economic performances are independent of political behaviours. Achievements of the economic compartment are affected by those of the political compartment, as has been seen in the previous section. Thus the economic equilibrium is subject to how politics works. Moreover, not only is the government's behaviour dynamic as policies change from year to year; but also it changes very drastically whenever the party in power loses its position as it is defeated in a general election. Then we have a series of equilibria through time corresponding to changes

⁶ L. Walras, Elements of Pure Economics, 1984, Lausanne (translated by W. Jaffe, 1954)

⁷ K.J. Arrow, General Equilibrium, Basil Blackwell, Oxford, 1983, pp.13-45 .

in governmental economic policies. What economists have to deal with is to examine whether this sequence is improving or worsening. But this is different from comparing a competitive equilibrium with any other disequilibrium point, on the assumption that there is no government compartment, as Arrow has done in his work on welfare evaluation of general competitive equilibrium.

Furthermore, we must not ignore the fact that as soon as we allow for the existence of the government and public production sectors, we must deal with, as Walras himself did, effects of their various regulations, such as price fixing, special privileges, monopolies and so on. These state interventions give rise to a deviation of the economy from the competitive equilibrium as was discussed by Walras himself. Governmental and public enterprises are not familiar with competitive economic circumstances, but lean upon advantages due to the state monopoly. Then it would be meaningless and misleading to compare the sequence of the performances of the private, economic compartment that corresponds to some government policies with the sequence of equilibria in the absence of government sectors by applying Arrow's welfare theorems.

It is well known that this tradition of economic analysis joins Keynes after the publication of his General Theory.⁸ Unfortunately, however, Keynes' formulation of the government is not dynamic. He himself and the followers of him too assume that the government's demand for goods is given and constant; then a pure economic analysis applies so as to obtain an equilibrium state of the private compartment of the economy. Then they introduce a hypothetical shift in the government's demand for goods and examine the effects upon the economy of this shift. This is nothing else but a comparative statistics analysis; no dynamic characteristic of the government decision making is taken into consideration in this Keynesian analysis. In spite of the incompleteness and insufficientness, the economists' view of the economy has barely been altered and improved by the work by Keynes into the direction of unifying economics and politics.

As has been said already, it is after Keynes that the government appears on the stadium, but only as a conductor (or a referee) of the game or a ground keeper, it is not involved in deciding victory or defeat of the game as a player. The government, however, is indispensable

for keeping the game in good order and preparing itself so that the game will become an exciting one. It was nine years after The General Theory that Attlee and Beveridge made the government a real player of the Game. Then we went into the age of mixed economy. Though it is usually taken as a mixed economy of capitalist and socialist economies, it is, in fact, a mixture of private and governmental enterprises. Such a view of the government originated from Italian economists. M. Pantaleoni insisted that the government revenues and expenditures should be accommodated into Walras' system of economic interdependence, U. Mazzola attached importance to the role of parliament, and A. De Vitti De Marco finally ascribed the crucial influence upon decision making of the government to voters.

Emphasis on the parliamentary democracy and the roll of voters in governmental decision making naturally results in leading to an emphasis on its dynamic characteristics. As has been pointed out, nevertheless, Keynes' treatment of the government was in a comparative statistics way. In the Keynesian economy, there are influences of the government on private enterprises, but no feedback from the latter to the former. By taking account of reciprocal interrelationships between the two compartments, private and public, of the whole economy, economists can at last get rid of the unnatural view of equilibrium theory that the economy eventually settles at a state of balance. As far as the society of human beings is concerned, there is no state of affairs in which all members of the society are satisfied, because except for extremely special cases there must always be some persons, probably many, who are not satisfied with what they are performing. They always want to improve themselves. Dynamics is a dear old house of economic entrepreneurs and politicians. They always bring unused resources into cultivation, so that we have a new frontier at all times.

8. There are nations whose peoples have only very narrow spectra of admissible political views. In one of such nations mild socialists do not form a single party of committed socialists, say, the Marxists. Then on the leftwing there may be two, three or more parties. Similarly, on the conservative side there may be Christian democratic, liberal democratic and even nationalist parties. Between these left and right groups of parties we may naturally expect several moderate parties, such as moderate and progressive liberal parties. In such countries that we usually see on the continent of Europe no single party can command a majority. A coalition cabinet is inevitable. Luckily it may be formed on the basis of two parties; usually it needs three, four or more parties.

⁸ J.M. Keynes, The General Theory of Employment, Interest and Money, 1936, Macmillan, London

Obviously political manifestos of the parties are not important for forming a coalition, because a party has to delete some items of its manifesto in order to accept some other items of another party. Negotiations are carried out among several parties. It is usual that there are still a few other possibilities of coalition, so that if one party is much too insistent in the negotiation, it is likely to be excluded from the coalition. Therefore, the agreed policies of a coalition cabinet are no more than a very unattractive mixture of policy programmes of the constituent parties of the coalition.

It is a product of compromise. It cannot be said to be a product of democracy because it is impossible to take the electorate's views or wills into account in the process of negotiation for the coalition. Strictly speaking, it is even impossible to say that the government has been democratically decided. In the worst case, the government's policy programmes may be a collection of the worst or insignificant parts of manifestos of the parties in power. Even so, any one of the parties is very powerful because if it insists on its withdrawal, then the coalition will be broken off. It is extremely difficult to get collaboration from all of these constituent parties, so that agreements between them are easily breached. The life-time of a coalition government is, therefore, generally speaking very short.

For such a country in which the people have a tendency to be divided into groups each of which forms its own party, the system of parliamentary democracy does not work well. Even though a fresh general election is held immediately after a collapse of a government, the newly formed government will also be a coalition one, so that it will be short-lived too. Repeating failures again and again, the people will naturally be disappointed in parliamentary democracy. Then a radical party will appear at last on the right or left wing of the parliament. As we have experienced after the First World War, the head of this party will become a dictator of the nation, and the people will lose all chances to be consulted by the government. A one way relationship in terms of order and obedience will be dominant within the nation. The people will prefer this militaristic life style to the previous lukewarm, liberal decadence. Then the government will put the private economic sectors under its subjugation. The free enterprise mechanism ceases to work in the private economic compartment. In parallel, the government and public sector compartment

becomes dominant, either corporatism, communism, or state economic control will prevail. The history will turn back from the age of free will to that of power. In the previous case of the two party democracy of the British type, the economy swings to and fro between the policies of the confronting major parties. In the nations in which multiple parties with all shades of ideology insist on their issues with each other, coalition governments are usually formed, so that they are short-lived. Eventually they trace out wider oscillations between 'democracy' and dictatorship. It is evident that the British type generous transfer of power between two parties is much stabler and safer than the one of sensitive choice of ideologies that allows for even dictatorship. This is a benefit of the people's generosity towards ideology.

9. Finally we have the case of one-party rule as we usually see in communist and ultra-right-wing parties. In these countries too, it is usual that freedom of political association is assured, so that the parliament has a few members of opposition parties. Their total share is certainly less than 10% of the total number of the members of the parliament. The government is never fearful of its motion being defeated. It is not wrong at all for communist countries to call themselves people's republics. Similarly, during the Second World War Japan had a party named the Imperial Rule Assistance Association (Taisei Yokusan Kai) which was a party for supporting the Emperor's rule. It is difficult for a politician not to be a member of it especially during the war period, because no one wants to be regarded as a person who does not support the Emperor's Rule, by saying that he does not join Taisei Yokusan Kai. Nevertheless, there were still a few brave men who kept the party at arm's length. Provided with such a huge association Japan was a country of yes-men during the war. Every motion submitted by the government passed the parliament by almost unanimous applause. The wars against America, Britain, China, Holland, and many others were declared in that sort of atmosphere. The national unity was never broken until the end of the war.

It is thus obvious that parliamentary democracy does not function properly unless an effective opposition party is working, so that the opposition must be regarded warmly and respectfully. It does not only act as a check on the majority party but also it may be a possible majority after the next election. To obtain a sustainable state of democracy, the government does not just implement the will of the majority; it has to implement the majority's will

subject to the checks by the opposition. Otherwise we cannot confine the government's performance within the reasonable bound set by the majority and the opposition parties, over a long period. As is often seen in countries on the European Continent as well as in the communist and ultra-nationalist countries, the rule of democracy is difficult to keep stable. They will eventually either collapse or turn out to be countries of dictatorship. To bring up a healthy, effective opposition party, the people must be strong enough to stand up for opposition. Moreover, they must be generous and not insist on detailed minor points; they must have a wide view of the essential matters and can be collaborative with each other. It is very difficult for a nation to be furnished with such a (rare) collection of personalities, so that there are nations which need a lot of effort to be politically successful as democratic countries. Nations have to begin with building up necessary ethos, if they are not provided with it by nature; it is a long way indeed.

It is without doubt that in order for a democratic regime to be established and successful both majority party and opposition parties should be able to work out a design for political innovations. To obtain this ability each of the major parties must have its own planning bureau where graduates from politics, economics and regional studies work to find out and design new political combinations. A majority without powerful new ideas is an obvious disappointment. Moreover, a new idea of the present opposition party must be designed so as to be well connected with the policies of the present government; otherwise, the power transition from the present majority party to its opposition creates nothing else than chaos. This means that democratic running of the government is indeed a very awkward one. We thus observe that the modern society consisting of two compartments; private-economic and public-political, has two engines for development which are fixed in respective compartments. The development heavily depends on the different kinds of mechanism working in these compartments. One is essentially competitive while the other monopolistic and directive.

In short, we may conclude in the following manner. Modern society must be structured democratically, but democracy is not sufficient but only necessary for establishing a sustainable workable democracy. In that sort of modern society where democracy prevails, the people are generally supposed to be liberal and insistent, so that their inclination to form a new political sect is strong. If so, each of most nations has a variety of parties; then the

government is likely to be formed on the basis of coalition, so that its lifetime is generally short. This means, the democracy's future is precarious in many countries, and unless they have a system of the British type, they always have to make a risky attempt on the knife-edge.

Finally, it is added that according to Gordon Brown's budget for 2000/2001, the tax burden for the same year is expected to be 36.9% of the national income for the same year. which is compared with the figure of 37% for the year 1999/2000. Similar figures for 1949 and 1969, taken from Hicks' The Social Framework are 21% and 26%, respectively, as I have already mentioned above. From these we realise there is a clear increase in the tax burden in the recent thirty years, 1969-2000. Although this period includes the period of Mrs. Thatcher's privatisation policies, it must be recognised that there has been a remarkably increasing demand for the product of the public-government sector. We may, therefore, conclude that the modern national economy cannot be dealt with by pure economic theory only. This is true not only in Britain but also in most other developed countries. Contributions of political decision making for the purpose of management of the national economy have greatly increased throughout the post-war period. This is not surprising because as Pareto has emphasised the society is formed on the two types of human sentiments antagonising with each other: sentiment of individual integrity (Pareto's residue V for economic egoism) and sentiment of group persistence (his residue II for altruism).⁹ If so, then it would be a great surprise if either of the two compartments due to respective residues overwhelmed the other in the national economy, so that our society is reduced to being purely egoistic or purely altruistic. This is really inconceivable.

I now conclude this article by referring to Max Weber's lecture,¹⁰ in which he appreciates passionateness towards realism as the most essential quality which politicians should have to obtain. The second most important nature that Weber attributes to politicians is that they should have a strong sense of responsibility. In addition they should not have a lack of a keen sense of proportion. If the leader of the ruling party is self-conceited because of his or her success in the past, then this has to be taken as an accurate warning to the effect that there is a high probability that the party will be defeated in the next general election.

⁹ V. Pareto, The Mind and Society, Vol. I, 1935, London .

¹⁰ M. Weber, Politik als Beruf, in Gesammelte Politische Schriften con Max Weber, 1938, Tübingen, pp.493-548.

