

Economic schools of thought: Labour perspectives

by Team itd

Table of contents

1. Overview	3
2. Background information	6
Introduction.....	6
Origins of economic theory.....	6
The classical school.....	7
Adam Smith.....	7
Historical background	7
The invisible hand	7
Division of labour	9
Theory(ies) of value	10
Ricardo's value theory.....	12
Karl Marx.....	13
Introduction	13
The commodities and abstract labour	13
Socially necessary labour time and the law of value.....	14
Surplus value.....	15
Small final note on capital concentration	16
Final notes on labour for the classical school	16
Neoclassical school (marginalists + Marshall)	17
Historical background & conformation of neoclassical school	17
From the labour value theory to utility theory	18
Marshall value theory	19
The creation of a labour market	20
The neoclassical understanding of unemployment	21
Keynes.....	23
Historical background	23
Keynes' critics to the (neo)classics	23
Keynesian new theories	25
The New Models.....	27
History strikes back	27
Friedman's return to (neo)classic	27
Neoclassics' school revisited: the theory of human capital	28
Institutionalism and new Marxism.....	28
Feminist economics.....	29

Ecological economics	30
Conclusions	31
New context, same orthodoxy spirit	31
The Theoretical Approach of the New Orthodoxy in Labour Economics	32
References	33
3. Training material	34
Activity 1: Bingo!	34
Activity 2: Quiz of value	37
Activity 3: True or false	39
Activity 4: Grouping the groupies	41
4. Interactive learning	45
Activity 1: Quiz of value	45
Activity 2: True or false	47

1. Overview

What are the different schools of economic thought?

Schools of economic thought, or simply economic schools, are groups of ideas that indicate how the economy works or it is supposed to work. The different schools (we are not talking about schools in the sense of colleges, institutes or universities but as lines of approach) have usually been named after the most prominent ideologist(s) that shaped its foundations and have later on added both supporters and detractors.

Since the origin of economics, many different kinds of economic schools have arisen. Undoubtedly, economic schools are continually changing and evolving. However, the main economic schools are commonly listed as: *Mercantilist school*, *Physiocracy*, *Classical school*, *Neoclassical school*, *Marxism*, *Austrian school*, *Keynesianism*, *Monetarism*, *Institutional Economics*, *Neoliberalism*.

In addition to these economic schools, there are many others of smaller size in terms of supporters and reach. At the same time, some schools have had offspring. Parallel schools have been developed on the foundations of previous ones with variations in some aspects, as Marxism builds on the Classical School as we shall see.

Which economics school is better?

While it is true that some economic schools have become outdated or incomplete over time, there are no better or worse economic schools. Ultimately, the affinity with an economic school depends fundamentally on the ideas of the author. An economist is not better or worse because he belongs to a particular school of economics. Some schools emphasise institutions, some on monetary or fiscal policy, some on growth, inequality, and so on. Some schools clearly have an ideological component. That is, they prefer one type of society to another. The most important thing, always, is to encourage debate between currents of thought in an argued and grounded way.

How does this article approach the study of schools of economics?

The main goal of this article is to present those theories that survived over time and that can inform us about current developments and economic policies. Thus, one cannot write on the issue of economic thought without focusing on the major economists of the past, that is, Adam Smith, David Ricardo, Karl Marx, and J.M. Keynes. The aim is to explore some general lines of their theories with special focus on the ideas regarding labour as the central axis to conduct the analysis. Based on these principal proponents the article also touches upon the neoclassic, monetarists, institutionalists and new schools of economic thought.

Pedagogically speaking it is much more interesting, and at the same time a deeper understanding of schools is expected to be achieved following a logical–historical approach. This means that each school is presented in the historical context of its emergence and analysed according to a logical rather than ideological criteria.

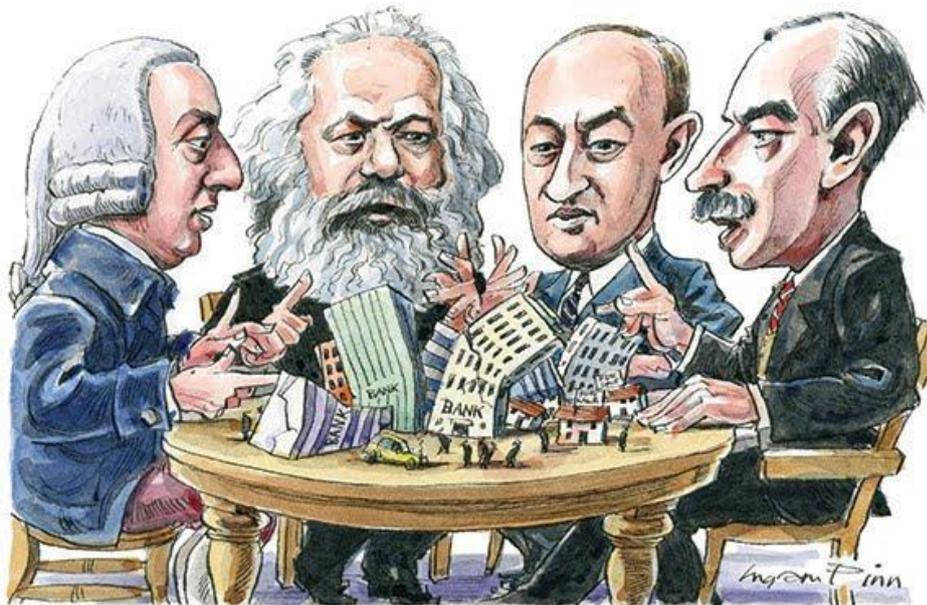
Why do we focus on labour?

Labour is one of the most important subjects discussed in economic theories. No less important, income from employment is the major source of individual income since the industrial revolution.

However, labour markets have been changing over the past decades. The rise in inclusion of women in the work-force has increased in unprecedented numbers, new technology has changed as well as income distribution, and labour conditions seem to be moving towards more insecurity, precarity and poor conditions of employment. In order to understand today's labour dynamics our approach takes a historical perspective that helps us understand the evolution of the concept of labour and its value, starting precisely with the first men that put the discussion on the table.

Why is it important to study the (old) schools of economic thought?

While present economic theories are the ones that govern the current economic system and therefore our lives, these theories did not appear out of the blue. In general, new economic theories appeared as a product of the elaboration of existing theories, or as a better answer to the persistent failures of a previous theory, that may just simply become outdated. The thing is, economic theory has no other 'testing terrain' rather than reality to prove its points. Therefore, in the economic field there is no better way to understand the present than to look at the past, in order to see current economic affairs in a fuller and more precise manner, while also enabling us to confront the reality of the future in a more prepared way. Ultimately, this not only stimulates one's interest to explore further the subject and its historical development, but also provides the reader with the necessary background to deal with more advanced current developments in economics.



First quick game: find out who these guys are?

KEYWORDS

Invisible hand

Use value

Exchange value

Abstract human labour

Socially necessary labour time

Surplus value

Utility

Marginal utility

Monetary illusion

Aggregate demand

2. Background information

Introduction

Origins of economic theory

The origin of Economics as a science is linked to the development of a new form of social organisation, capitalism, a system that solves the organisation of production and distribution through the expanded functioning of the markets. Markets are therefore the epicentre of capitalism as they encompass the operation of the entire economy.

Capitalism was established through a long and slow process that started in Western Europe in the 16th century and gained momentum with the advent of the industrial revolution in the mid to late 18th century. This is not to say that the capitalist regime would have replaced feudalism because a group of "inspired" individuals found the key to invent the automatic loom, the steam engine, and the smelting of iron. On the contrary, it was the junction of three novel phenomena: the universalization of exchange, a more pronounced division of labour, and the appearance of numerous and substantial technical advances that let capitalism begin to dominate. This was the argument of Adam Smith in his book *The Wealth of Nations* (1776), where he established the bases of the economic theoretical system for which he is known as the father of modern economy.

In fact, it is the first of these three concurrent elements, exchange, that according to Smith is the central (natural) element present in the human DNA and becomes the engine that drives the entire process of social transformation; the other two appear as a consequence of its deepening. Considering exchange in the market as the main axis of economic activity, it became necessary to discover the source that determined the proportions of exchange and the circumstances that could provoke the apparently erratic evolution of the prices of goods. The answer was found in a fundamental concept, *value*, whose origin and measure, according to Smith, was in labour:

"Labour, therefore, is the real measure of the exchange value of all kinds of goods" (Smith, 1958, p. 31).

The differences in the consideration of labour as a source of value, even in the readings of Smith or Ricardo and of course in that of Marx, all labelled under 'the classics', is the axis around which this paper organises its analysis of the schools of economic thought. If capitalism's central virtue is to transform all productive resources into goods, those resources, such as capital, land and labour appeared, as well, organised in markets for the factors of production. This implied that labour, under the new wage-earning regime, was also transformed into a commodity. Thus, it was natural that questions about labour's value and price, its use and the conditions under which better it could contribute to the creation of wealth as well as how to distribute it, began to appear. All these issues were not easy to conciliate, especially for the blossoming economic science that developed in a context of a new type of social conflict characterised both by its potential and by involving social classes objectively defined by their position in the production process.

The analysis of labour as an entry point in the different schools of economic thought is presented as subsumed in that of the general historical contexts and conditions in which the different schools based and formulate their theories. After exploring the Classic School (Smith, Ricardo and Marx), we introduce the Neoclassical school of thought in which we deepen in the distinction between

marginalist and Marshall. Then we follow the critics and new proposals of Keynes, and later on the New schools segment under which we explore the different lines that have derived from the main schools. In the end, we propose some conclusions on the current situation in terms of dominant schools and ideologies and how that affects today's labour structures.

The classical school

Adam Smith

Historical background

The Wealth of Nations (1776) is the book that made Smith famous and established him as the Father of Economics. The content of the book is truly revolutionary if we take into account that it was written during a time period in which feudalism was still widespread and also quite strong, and that the part of the economy that was organised according to the market mechanism was extremely small, albeit rapidly growing. In fact, Smith's contribution is located precisely in the final stage of the transition from a mediaeval and feudal society into the modern and capitalist one. More specifically, it is usually identified at the end of the 18th century, especially when it comes to England (and, by extension, Scotland), with the beginning of the industrial revolution.

At the level of production processes it was manufacturing production that gave impetus to the consolidation of two of the social classes characteristic of modern society: the industrial capitalists, on the one hand, and the industrial proletariat, on the other. Nevertheless, despite its fully modern features (such as the new productive modalities in the labour fragmentation and specialisation) the manufacturing production that Smith witnessed was far from mature. The industrial revolution had recently started but was still unfinished.

The categorical break that Smith produced in the defence of the nascent capitalist system must be considered, more than anything, as a reaction and a critique of traditional, mediaeval, feudal and absolutist systems that governed until that time. Smith's intentions to discover the laws that ruled the new modern society definitely broke with the scholastic tradition fundamentally permeated by theology; while also rejecting some of the main propositions of the two economic currents that date from the immediately preceding centuries and that also belong to modernity: Mercantilism and the Physiocratic school. In other words, beyond Smith's class membership, modern society's apology can be interpreted as a result of its rejection of the hegemonic traditions of the time.

The first great question that Smith pursued was to reveal the mechanism through which a social system of the type outlined above would function over time and remain stable. In the next section we touch upon some of the ideas and the "economic laws" that Smith used as arguments in defence of the new social regime from a "scientific" perspective.

The invisible hand

By introducing the notion of economic laws and their operation, Smith placed economics on a scientific foundation. This is the reason why he is called the founding father of modern economics. In concrete, Smith intends to show that the economic forms of the capitalist system, not being governed

by traditional principles and norms, meaning by feudal regulations and restrictions, do not lead to a general disorganisation but, on the contrary, capitalism is governed by a set of laws that ensure the material reproduction of society and, furthermore, its progress. However, these laws have a particular nature.

First, Smith outright dismisses any immediate link between economic laws and divine laws. On the contrary, economic laws refer to a purely human phenomena, and more specifically to the **self-interest** of humans. Smith argues that self-interest, a socially unacceptable motive, gives rise, via complex social interrelations, to social cohesion and to growth.¹ Considered from a strictly individual perspective, if a certain way of acting is more profitable or satisfactory, and the same happens with each one of the individuals that make up society, then, by virtue of that individual convenience, such behaviour and its results are the ones that will be imposed as general economic laws. Smith described this spontaneous operation of objective laws that guide human action in a way that accords to the interests of society as a whole as the **invisible hand**.²

While one would expect that self-interest would lead to a chaotic society, Smith instead argues that society does not collapse thanks to **competition**. When each and every member of the society seeks to serve his or her own interest, without regard for social costs, his or her interest confronts with those of other similarly motivated individuals. If, for example, a producer charges a too-high price, then it is expected that the buyers will turn to other producers. If a producer underpays his workers, workers will seek employment elsewhere.

In addition, this system is based primarily on decentralised decisions of numerous individuals without the mediation of any central coordinating agency but only under the coordination of the market mechanisms that solve the problem of production. For example, if the price of a product is too high, this is an indication that society wants larger quantities of that product. High prices give rise to excess profits, which attract investment in this profitable activity; this accumulation of capital expands the supply of the product, something that society wanted in the first place and at lower prices. The converse process takes place in the case where the price is below normal. In the same line, the problem of distribution is implicitly solved, since the prices of the products incorporate the normal rewards of the factors of production, that is, normal wages, profits and rents.

In short, Adam Smith grounded his theory in the entwining notions of self-interest and competition which led by the invisible hand explain how the market mechanism is a self-regulated system, whose operation does not lead to chaos and to eventual breakdown, but rather to a system that manages to give rise to social cohesion and to hold together all centrifugal forces.

¹ He grounded his the case in a previous publication, *The Moral Sentiments* (1759)

² "As every individual, therefore, endeavours as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor he knows how much he is promoting it. By preferring to support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it". (WN, p. 423)

Division of labour

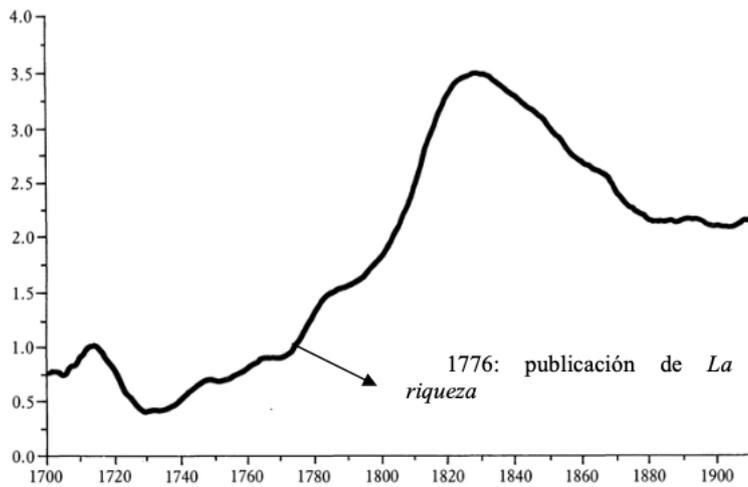
In *The Wealth of Nations*, Smith's search for understanding of the new dynamics of the 'civilised society', that is to say, of the nascent capitalism whose birth he was witnessing, is an intention to find an answer to the natural follow-on question: "what is wealth?". In fact, Smith's responses showed immediately, since in the first sentence that appears in the book's introduction he makes a brief statement that arguably would become the cornerstone of the entire classical theoretical system:

"The annual labour of each Nation is the fund that in principle provides it with all the things necessary and convenient for life, and that the country consumes annually. Said fund is always integrated, either with the immediate product of labour, or with what is purchased through said product from other nations."(WN [1776] p. 3).

Briefly, almost laconically, Smith brings essentially different two points of view from the two most important theories of his time. In the first place, he maintains that wealth is made up of goods, of products of all kinds - the "necessary and convenient things for life". And secondly, and even more importantly, he asserts that the sole and exclusive source of wealth is men's labour, or more precisely, the labour of the society taken as a whole - the "annual labour of the nation". He explicitly rejects mercantilist ideas that argued the origin of wealth should be sought in commercial operations and its preferential form is money; as the belief of the mercantilists stated. But neither is it created solely by agricultural work nor does it take shape exclusively in the primary products generated by nature and which will then undergo various transformations, as was defended by the Physiocratic version.

Continuing with this reflection, if it was true what Smith maintains - that is, that wealth is made up of things necessary and convenient for life and whose origin is labour, the next question that the author tried to answer was "how could a society increase wealth?". Smith's argument was a direct follow-on from the above, as he stated that the natural tendency of the market economy is the growth of wealth that is created from **the division of labour** with its consequent increase in productivity and reduction in cost. Here again, it is important to remember that Smith was describing an economy in transition from feudalism to the market system. Smith's time is characterised by the diffusion of manufacturing production and not by the appearance of the modern factory and its technological innovations. This implies that the increase in the volume of production should be unequivocally attributed to a growth in the "productive powers of labour", since it was not associated with either a substantial increase in the working population or the use of new machinery to assist the worker in his tasks. The cause of the increase of labour productivity must be then sought, according to Smith, in the deepening of the division of labour.

Gráfico 1. Tasa de crecimiento del producto industrial de Inglaterra 1700-1913



Fuente: Crafts y Harley (1992)

Graph: the growth of industrial production in England 1700-1913

With the purpose of explaining the division of labour, for which Smith uses the famous analogy of the pin factory, he explains that when the production process aimed at the manufacture of the same article is fragmented into numerous simple operations performed by different workers, an increase in labour productivity takes place for three reasons: First of all, the specialisation of the worker in a single repetitive task gives him greater dexterity; secondly, there is a saving of the “downtime” caused by the passage from one operation to another; and finally, by dedicating the whole day to a single task, the worker’s creativity is stimulated, which helps you to devise new and more effective tools of work or to improve old ones.

This labour division theory adds two important elements. First, although the market society functions in a completely decentralised way, where each individual seeks to satisfy his own self-interest, yet this society creates internal mechanisms that bind people together in a cohesive totality. Far from establishing total independence among producers, a relationship of mutual dependence, of a new type, is established among all men: “*in a civilised society - Smith says- [every man] needs the cooperation and assistance of the crowd at every moment*”(WN [1776] p. 16). Secondly, Smith demonstrated that such a society is capable of economic growth, as the division of labour unquestionably leads to a rapid increase in productivity, which in turn leads to the growth of the economy. The next question is whether this growth of the economy will continue forever, an issue that Smith relates with the supply and demand of labour and its price, for which we need to understand Smith’s theory of value more in depth.

Theory(ies) of value

It has already been established that civilised society is in its essence a commercial society, in which, as a result of the division of labour, each man specialises in a form of production and is therefore obliged to resort to the product of other men's labour through exchange. The line of argument drawn in the *Wealth of Nations* leads to the discussion about the forces that govern exchange relations, that is, the determination of the value of commodities.

The theory of value is the effort to connect the surface phenomena of economic life to some inner law. Smith affirms that the word VALUE has two different meanings, since sometimes it expresses the utility of a particular object value, and, at other times, the ability to buy other goods. We can call the first **use value** and the second **exchange value**. The starting point of the investigation is precisely the question: how is the relative value or exchange value of goods determined? What Smith said is that exchange value is not quantitatively conditioned by use value (by utility), and that the magnitude of use value and exchange value are two independent factors of the commodity.

Smith argued in the first three chapters that labour is socially divided in such a way that for the owner of a commodity - dependent on the labour of others to obtain things necessary and convenient for life - the value of his commodity is equal to work of others that your merchandise allows you to acquire or "command" in the exchange. According to Smith, when an individual exchanges one commodity for another, he is actually acquiring someone else's work "embodied" in that product. Therefore, the value is, essentially, labour, and its magnitude is fixed by the amount of needed work. Nevertheless, here he faces one of the many difficulties in the race for discovering the real meaning of value. As much as it maintains that labour is the only true source of value, the truth is that labour cannot be observed by itself, which leaves a second question: how is this labour measured?

The simplest way to guarantee the result would be that the individuals involved in the exchange knew the quantities of labour contained in the commodities. For that, Smith takes the radical approach of describing a primitive society in which there is neither capital nor wage labour and where the worker-producer knows exactly the amount of work that each product of this society involves:

In the primitive and crude state of society, which precedes the accumulation of capital and the appropriation of land, the only circumstance that can serve as a norm for the reciprocal exchange of different objects seems to be the proportion between the different amounts of labour that it is needed to acquire them. If in a nation of hunters, for example, it usually costs twice as much to kill a beaver as it does a deer, the beaver will be naturally exchanged for or be worth two deer. It is natural that generally the product of the work of two days or two hours is worth twice that which is the consequence of a day or an hour (WN [1776] 1997: 47)

So in this context the law of value based on labour is fulfilled. Smith thus achieves his goal, only that he does it at the cost of making the law of value lose all its theoretical interest, since it would be a law that describes the behaviour of prices only in primitive society. What is, then, the law that governs exchange – the value exchange - in today's "civilised society"? To answer this question, Smith had to abandon the labour theory of value and proposed a completely new and different explanation, known as the *adding-up theory of value*, which maintains that the exchange value is determined by the sum of wages, profits and income, that is to say, the rewards obtained by all those who participate in the production process: workers, capitalists, landowners. This theory of value, known as well as the "theory of production costs", in fact, constituted a theory of price determination based on the cost of production, which was to play an important role in our days. This notion of value became the starting point for the development of theories of value that place labour, capital and land as equivalent factors of production and creators of value. This interpretation was supported by many economists of the nineteenth century, who include J.B. Say and J.S. Mill.

Ricardo, as we will examine in the next chapter, adopted Smith's first view of value known as the labour theory of value and made an effort to apply it to modern society and solved some of the riddles that made Smith abandon his first (and correct according to Ricardo) view.

Ricardo's value theory

David Ricardo's kind of influence on the history of economic thought was quite different from that of Adam Smith. In the first place, Ricardo managed in life to form a true school of economics of which he was the undisputed leader. To frame the context, Ricardo's time was four decades after Smith's contributions. Therefore, he was indeed able to witness the development of a capitalism moving rapidly towards maturity, where the forces of the industrial revolution had already been unleashed in an irrepressible way. Moreover, precisely as a result of his position in the history of ideas, Ricardo had a privileged point of departure for his own investigations: Smith's *Wealth of Nations*. He stands on the shoulders of a giant.

Ricardo's major contribution to the theory of value is his insistence on the acceptance of Smith's labour theory of value, according to which the relative prices of goods are approximately proportional to the relative quantities of labour that were spent for their production. Concretely, in Ricardo, the labour time is the primary regulator of natural prices, which in turn are the centre of gravity of market prices:

All the great variations which take place in the relative value of commodities to be produced by the greater or less quantity of labour which may be required from time to time to produce them. (Works, vol. I, pp. 36–37)

Ricardo's disagreement with Smith is clear. Smith was forced to abandon the labour theory of value in the face of the rise of a capitalist society in which he could not explain the reasons for the difference between the commanded labour (wage) and incorporated labour (product value). Ricardo's critique indicated that the salary is not - it cannot be - equal to the value of the product but is governed by other laws, since the salary, like the price of any other merchandise, is subject to permanent variations. The "value of work", that is, the amount of the salary, Ricardo maintains, does not contradict or invalidate the determination of the value for the working time and is not related to the magnitude of the value of the product.

If the determination of the labour value theory is fulfilled, a change in wages is incapable of modifying prices, as long as the labour time requirements of each product have not changed. However, the variation must be absorbed in some way, and in effect it is because profits are, according to Ricardo, an inverse relationship with wages. The value is determined by the amount of labour, but then this value must be "resolved" into wages and profits. As wages vary, the total magnitude of value does not change, says Ricardo, but its distribution between classes does. The consequences of this simple conclusion are big: on this basis it must be accepted that capitalist society is inexorably traversed by a distributive conflict between capitalists and workers. The opposing interests of one and the other face them fatally: any increase in wages necessarily implies a reduction in profits. When Smith came across the mutual relationship between wages and profit, he abandoned the theory of labour value to embrace that of production costs, which only nullifies the conflict since, according to this approach, increases in wages cause increases proportional to commodity prices, rather than determining a general drop in profits. Harmony reigns then - with the notes that we indicate - between employers and workers.

In spite of the lack of a perfect invariable measure of value, Ricardo accepted the principle according to which the exchange ratios of products (meaning goods prices) are regulated by relative labour times expended in their production not only in 'the primitive society' but also in capitalism. The difference is that in capitalism, the labour theory of relative prices needs several qualifications and modifications.

These modifications relate to the presence of factors such as capital–labour ratios and changes in income distribution.

On a final note, Ricardo showed particular interest in questions of international trade. He thought that his labour theory of (exchange) value could be extended to include not only domestic but also international markets. Added to that and by using the quantity theory of money, he derived the principle of comparative advantage, an idea that has survived (albeit modified) until our days and can be found in all books of international trade.³

Karl Marx

Introduction

From the point of view of the history of economic thought, at the end of the 1860s and the beginning of the 1870s, two currents that proposed to break with classical political economy were born. Two movements that, however completely opposed and simultaneously (with a difference of a few years -Marx, in 1867 and the Marginalists 1870), gave its almost definitive shape to the scene of contemporary economic theory.

Marx's perspective does not consist in rejecting exhaustively all theories formulated by the pillars of the classical political economy (Smith and Ricardo); but he takes them as its starting point. However, Marx's objective is to transcend the classical legacy, preserving in part its content but also pointing out its limitations. The importance that Marx himself attributed to the works of Smith and Ricardo is also manifested in the numerous quotations included in *Capital*, but also in the detailed analysis that he dedicates to them.

There are different interpretations of Marx, and this often gives the impression that his work is a political pamphlet. This is indeed connected to the history of the socialist movement, the origins of which were inspired to a great extent by Marx himself, more specifically by the political and philosophical writings of Marx and Engels (e.g., *The Communist Manifesto* (1848), *The German Ideology* (1845–1846)). Nevertheless, this narrow interpretation would ignore Marx's major economic contributions, that is, the three volumes of *Capital*.

The commodities and abstract labour

The goal of Marx's economic studies was to "*lay bare the laws of motion of modern society*" (*Capital*, vol. I, p. 10), that is to say, to discover social regularities described mainly as long-run tendencies. Marx observes that capitalism is a historically specific system characterised by generalised commodity exchange, so, naturally, the starting point of his inquiry is the analysis of commodities, the most elementary form of the wealth of a capitalist society. As the classic school already pointed out, commodities have a dual property: they can be used to satisfy needs and they can also be exchanged. Adopting the established terminology in Marx's time, a commodity is at the same time a *use value* and *value*. Again the question posed is: what regulates that exchange?

If the commodities did not have in themselves "something equal", they could never be equal in exchange, and that something equal has nothing to do with their respective *use values*. This is because

³ For more information about this, see the chapter on Competition or Cooperation.

their material bodies, their use values, far from making them equal, make them different from each other. When the use value of goods is abstracted, there remains a single common property: all of them are products of labour, but of labour considered as indistinct labour. Commodities are values because they represent the **abstract human labour** that produced them.

When Smith, originally, and later Ricardo, struggled to find what "created" value (the source of value), they came to a conclusion, as original as it was difficult to demonstrate: only and exclusively labour has the capacity to "create" value. Once this finding was established, they proceeded to postulate that there was a proportional relationship between the value and the labour "contained" in the commodities. In this field two crucial differences between the classics and Marx must be pointed out. In the first place, the classical authors always refer to the labour without making further clarifications. They thus confuse two aspects of labour: labour considered as human productive activity in general (what Marx calls abstract labour); and the activity aimed at manufacturing a certain product (useful and concrete labour). These are not two different activities, but two different ways of looking at the same job. In other words, Marx calls the total quantity of abstract labour time, that is, incorporated in a commodity the immanent measure of *value* of the commodity.

Secondly, classical political economy was confined mainly to how price, or in other words the exchange value was established. Unlike the classics, Marx has never said that this quantitative determination of value is immediately comparable with the relationship that exists between observable prices in the market. Remember that for both Smith and Ricardo the categories value and exchange value (or price) are confused until they become one, as if it were a single phenomenon. For Marx, value and exchange value are not the same, contrary to what Smith or Ricardo believed. Consequently, labour should not be confused with value just as value should not be confused with price.

Socially necessary labour time and the law of value

The value of a commodity is equal to the quantity of the abstract labour time that is socially necessary for the production of the commodity in question. Hence the notion of socially necessary abstract labour time is different from the homogenised labour time of Smith and Ricardo.

For Marx, the quantity of labour and, consequently, the magnitude of the value, is determined by the labour time required to manufacture any commodity, that is, by the labour time required on average to produce it or, in other words, by the labour time *"socially necessary required to produce any use value, under normal conditions of production and with the average degree of skill and intensity of work prevailing in society"*. For example, Marx (Capital, vol. I, p. 39) refers to a characteristic example that was observed in England when the introduction of power looms reduced the socially necessary labour time for the production of cloth by about fifty percent. The traditional producers who continued working with hand looms found out that the value of their commodity was slashed by one-half not because of the reduction of their own labour time but because of the reduction of the socially necessary labour time.

How does the magnitude of the value vary? If more work is required in the production of a certain commodity, the greater its value. And in the same way, the greater the productive capacity of labour, the smaller the magnitude of the value, since the amount of work invested in the production of each unit will be less. In short: *"the magnitude of the value of a commodity changes directly to the quantity of labour and inversely to the productive capacity of the labour invested in it"* (Capital [1867] 1986: 8).

Following this logic, the law of value – according to which the socially necessary labour time is directly embodied in a commodity – is the regulator of the movement of market prices. Prices are the means through which capitalists realise their profits and losses and regulate their behaviour accordingly. Socially necessary labour time constitutes the regulator of prices and profit and, therefore, of social reproduction. The operation of this dual relation is what Marx calls the law of value whose role is analogous to Adam Smith’s “invisible hand”, for it provides an explanation of how the capitalist society reproduces itself and the various scales of its reproduction.

Surplus value

Marx made the distinction between labour and *labour power*, a distinction that is absolutely crucial for the understanding of the concept of surplus value.

Labour-power or capacity for labour is to be understood as the aggregate of those mental and physical capabilities existing in a human being, which he exercises whenever he produces a use-value of any description. (Capital, vol. I, p. 186)

It follows then that labour is the utilisation of labour power, that is, of the useful labour that a labourer performs in a specific period of time. And, like any other commodity, the value of labour power is determined by the amount of labour that its production requires. In this case, the magnitude of value is equal to the labour time required to produce the worker's livelihood. In other words, the value of labour power is equal to the socially necessary labour time required for the production of commodities that a worker purchases with his money wage to reproduce himself and his family. But the labour time embodied in the commodities normally used by the worker for the reproduction of himself and his family in a day is less than the labour time that a worker actually offers to the owner of capital during the same time period. The result is that for any given time period, the worker produces more value than the wage equivalent which is paid by the owner of capital for the use of the labour power. This difference, Marx calls “unpaid labour” and “surplus labour”.

This argumentative line, starting in the analysis of the commodity and continuing to the ideas of abstract labour, social necessary labour time and labour power constitute the theoretical cornerstone of Marx's political description of the modern society. For Marx, all societies require labour to reproduce themselves. So much so, that in all societies a particular social class performs more work than what is required for its own reproduction with the excess labour being appropriated by the dominant classes through property relations, traditions, the legal system and also force. Such exploitative relations are quite transparent in pre-capitalist modes of production (e.g., slavery and feudalism), whereas in capitalism they are embedded in monetary transactions that give the impression of equal, and, therefore, fair exchanges.

The difference between total labour time and that required to reproduce the workers' capacity to work is called surplus labour time and its monetary expression, the *surplus value*, is appropriated by the propertied classes (capitalists and landlords) and the state. The wealth accumulated in a society is directly related to the amount of surplus labour time, which is inversely related to the necessary labour time of the labour power. The distinction between labour and labour power is Marx's greatest discovery and contribution to political economy, because through this distinction the source of surplus value can be explained.

Small final note on capital concentration

To obtain a complete picture of Marx's system, the full development contained in *Capital* should be explored, which is beyond the scope of this article. Nevertheless, apart from the theory of surplus value, one more thing is essential to take away from Marx's *Capital*, the idea of *capital concentration*.

According to Marx, the hallmark of the individual behaviour of capitalists is the pursuit of profit as a purpose in itself, which forces them into two kinds of competition: the first with workers in the labour markets over wages and conditions of work, and the second with other capitalists in the commodity markets over the expansion of market share at the expense of their competitors. Capitalists cope with these two types of competition through the introduction of more fixed capital. As a consequence, mechanisation of the labour process is used to raise the productivity of labour. The introduction of fixed capital both increases the scale of operation needed for minimum efficiency and reduces the unit cost of production. The latter implies that by reducing their prices, innovative firms are able to expand their market share at the expense of less efficient firms. Thus, the process of capital accumulation leads to a small number of top firms controlling an increasing share of the total market. This is the reason why concentration of capital is the expected outcome implied by the nature of capital and by the operation of competition, which by no means diminishes over time.

If there is a grand prediction that has been historically validated, it is Marx's law of increasing concentration of capital.

Final notes on labour for the classical school

Our goal here is to clarify the structure of classical theory and more specifically point out specific aspects of this line of thought that will later on be taken by the continuing and opposed schools of economic thought. To begin with, classical economics is a term invented by Marx and later on taken by Keynes. According to Marx, the shared common point of all the thinkers that could be grouped under the term of classical economist is the view that labour employed in production (in general) is responsible for the creation of value. Nevertheless, as we have seen, these common views still resulted in many differences between the classical thinkers.

Now, there are some other points about the classical economist and its methods of analyses that should also be mentioned. In the classical analysis there is no assumption about the full utilisation of the labour force. The unemployment of the labour force coexists with the normal utilisation of the economy's productive capacity (which is utilised at its full potential in the longer run). The existence of underemployment appears in Ricardo as well as in Marx in his notion of industrial reserve army. On the one hand, for the classic school the level of employment (or in other words the quantity of labour) was determined by the level of capital accumulation (and its capacity to demand labour) and by the variation of the population. On the other hand, wages (or in other words the price of labour) were determined by the idea of the cost of the worker's reproduction (meaning the basket of goods that workers normally purchase).

This is characteristically different from the neoclassical theory, as we shall see, for which this process is defined in the *labour market*, where the prices (level of wage) and quantities (level of employment) are determined by the demand and supply forces.

Neoclassical school (marginalists + Marshall)

Historical background & conformation of neoclassical school

During the first half of the 19th century a fierce confrontation developed between the industrial bourgeoisie and the old landed aristocracy. The political discussion was marked by the confrontation between the protectionists and the free traders, between the countryside and the industry, that is, by the brawls typical of the period of consolidation of capitalism. Gradually, along with the advance of capitalism, the axis of the conflict between the classes continued moving until it took the form of an increasingly open conflict that has the working class as one of its protagonists.

In its beginnings, the conformation of the factory system had found an almost inexhaustible deposit of peasants, serfs and vassals expelled from their lands and impoverished artisans to fuel the “deposits” of an eminently weak and disjointed proletariat. The so-called “original accumulation”, the starting point of the capitalist regime, was marked by unlimited exploitation of the new salaried workers, whose associations were prohibited and their claims were persecuted and punished. It was not until the third decade of the 19th century that the working class began a resistance movement.

Arguably, economic theories were forced to accompany this system changing cycle. Indeed, in the field of economic thought, the period began with the agitated controversies between supporters and detractors of the Ricardian system, the one that has consolidated as the hegemonic orthodoxy.

Throughout the second half of the 19th century, from 1850 to 1870, the political economy seemed to stabilise, forming an orthodoxy with Ricardian roots and with John Stuart Mill, Ricardo’s pupil, as the dominant figure. However, under the surface of broad consensus, the two new theoretical systems that would mark the theoretical terrain during the 20th century were developing: the Marginalist system and the Marxist system (parallelism already introduced in the first section of Marx). Marginalism became a new orthodoxy that devoted many efforts, especially at the time of its consolidation, to confront the ideas of Marx.

This initial stage was a genuinely revolutionary stage for Marginalism, as its promoters set out to dethrone and displace the orthodoxy of that time, that is, the classical school of “Ricardo-Mill line”. With the difference of a few years, the three founding works that gave shape to the Marginalist movement were published. These books are the *Theory of Political Economy* by the British William Jevons (1871), the *Principles of Political Economy* by the Austrian Carl Menger (1871), and the *Elements of Pure Political Economy* by the French Leon Walras (1874).

The ideas of the ‘marginal economists’ gradually formed an integrated theory, which has been called neoclassical economics. The triumph of the movement, nevertheless, was not achieved by the three founders but came by the hand of Alfred Marshall. In 1890 Marshall publishes his *Principles of Economics*, giving a more mature and complete expression to the contributions of marginalism; but, this maturity was reached at the cost of smoothing out certain “rough spots” and attenuating - even making it disappear completely in some cases- the polemic argumentations of the three Marginalist predecessors. Marshall proposed a kind of synthesis between the Marginalists and the classics becoming, therefore, the architect of the neoclassical school of thought. Marshall argued that the ideas of the marginal economists are merely the evolution of the classical economists and in this sense they are *Neoclassical economists*.

From the labour value theory to utility theory

In our discussion of the structure of the classical theory, we found that the core of this theory is based on the theory of value based on the labour time, or in other words the labour value theory that explained the value-exchange (price) of commodities. In order to understand what led to the replacement of this theory by the neoclassical theory based on utility, we need to bear in mind the intellectual atmosphere that was developed in the middle of the nineteenth century. During this time period there was a rising concern with the labour theory of value as it was attracting discontent from the establishment that thought that the theory was bringing socially dangerous conclusions and finding strong support among a number of socialists and, in general pro-labour, economists. Looking backwards, we can understand how the new neoclassical utility theory's very purpose (stated or not) was to set aside the classical approach because of its disturbing political implications emanating from the labour theory of value and its association with Marxism and socialism. The idea that the value of commodities is determined by their labour content was too challenging for a system that underwent a structural transformation.⁴

Around 1870, the classical theory of value had, strictly speaking, two different versions: the determination of value by the quantity of labour (Ricardo) and the more widespread determination of value by the costs of production (Mill). Opposed directly to the production-value theory, the axis of Marginalist analysis consists in studying the determination of value exclusively at the moment of the exchange. The subsequent ideological and theoretical controversy crystallised by the marginalism, affected the theoretical consideration of labour. What Marginalist claimed was that, instead, the value of a commodity was determined by its *utility, a concept* that refers to the satisfaction of an individual that derives from the consumption of a good or the use of a service.

So what "gives value" to objects, is the way in which men "value" goods as objects destined for consumption, capable of satisfying their tastes and needs. A substantial difference, of origin, is thus established with the classical system, where it was assumed that the goods arrived at the exchange process with a "value" determined by the conditions of production (either by the amount of labour or by costs of production). By replacing the centrality of *value* in order to make it of *utility*, the centrality of labour in economic discourse was lost and theoretical analysis could ignore the problem posed by considering the distribution (wage/profits) of the surplus in the manner of the classics.

The major contribution of the Marginalists, and the reason that gave them that name, was the concept of *marginal utility*, upon which the definition of the demand curve was shaped and remains until our days as the basis of the microeconomic line. For the Marginalists, the demand depends on the marginal utility, that is, the utility derived from the consumption of an additional unit of the good in

⁴ Industrial capitalists, up until the middle of the nineteenth century, were directly involved in the production process in their incessant pursuit of expanding profits as a purpose in itself. The labour theory of value contributed to the understanding of the source of profit as well as the source of incomes for the merchant and the landlord classes. As a result, the labour theory of value was the product of, and at the same time contributed to, the intellectual atmosphere for about a century. However, the growth of corporations and the subsequent concentration and centralization of capital that took place during the depression of 1873–1896 changed the structure of the economy as well as the role of the capitalist. The capitalist's direct involvement in the production process and other related activities was limited and the management of the newly created large-scale enterprises was transferred to a small group of owners or professionals. As a consequence, the capitalist class was transformed, to a great extent, into a mere recipient of profit incomes by virtue of property rights in a way similar to that of landlords. Naturally, under these new conditions, it became clear that profit income could not find justification in a labour content explanation of equilibrium prices, other than some form of exploitation of labour.

question. It was claimed that as the consumption of a good increases, the satisfaction that a consumer derives from the consumption of successive units of the good in question progressively diminishes. Consequently, the consumer would be willing to pay a lower price for higher quantities of the same good. Thus, we may construct a typical demand curve, that is, a schedule between prices and quantities, with a negative slope precisely because it reflects the law of 'diminishing marginal utility'. Hence, the value comes entirely from marginal utility, which is a "measure" of the pleasure that its consumption provides, a pleasure that is reduced when the quantity consumed increases. The next step is to aggregate these individual demand curves to arrive at the market demand curve.

The Marginalist theory of value should have been complemented by a Marginalist theory of distribution, that is, by the set of laws that govern the determination of wages, profits and rent. The truth is that the first three Marginalists failed to reach an agreement on these new laws, as opposed to the unanimity reached with marginal utility theory. It is precisely in this less complete segment of Marginalist theory that Marshall comes to the rescue to offer us his theory of value (closer to Classic school) as we will see below.

Marshall value theory

When we examined the original "revolutionary" proclamations of the first three Marginalists (Jevons, Menger, and Walras), we reproduced some of the ideas with which they attacked the Ricardo-Mill school. As we mentioned in the introduction, for Marshall, the Marginalist and the classical are two partial and incomplete versions of the same theory of value. Marshall's goal was, then, to reconcile the classical school with the novel theory of marginal utility. For Marshall, the main contribution of the Marginalists is limited only to the study of the foundation of the downward sloping demand curve based on the marginal utility theory. However, he argues, the principle of marginal utility cannot be taken as a law of value.

Instead, Marshall affirms following the classical line, that to make the decision regarding the quantity to be produced and brought to the market, the producers do nothing other than estimate their profits calculated as the difference between the price of the demand (how much they would be paid) and the cost price, including wages and profits in the latter.

The principle of cost of production and that of final utility are undoubtedly component parts of the general law of supply and demand; each of them can be compared to a blade from a pair of scissors. (Marshall [1890] 1948a: 682).

Following this line, Marshall then faced the question of determining the "costs of costs", or in other words the *real costs of production*. Here lies the most profound content of Marshall's theory of value: hidden behind the prices of all commodities are, the two original types of "sacrifices" that men must go through to produce them, the *sacrifice of labour* and the *sacrifice of waiting*. The idea that labour is a source of value, as we saw, has a classical ancestry, although here the emphasis is not on work as a "cost" due to the physical exhaustion or to the expenditure of energy, but to the "psychological" sacrifice that means to work. More specifically, wages are no longer theorised as the cost of reproduction of workers – clearly, a classical idea – but rather as the "disutility" that a worker suffers by offering his labour services. Along with the sacrifice of the worker comes that of the capitalist. "The wait" to indicate that when a capitalist allocates his wealth to production and not to consumption he experiences suffering and, therefore, deserves a retribution (the interest rate). Then, profits are

viewed as the disutility of the entrepreneur, who by abstaining from consumption manages to save resources in order to invest them and profits are the compensation for this sacrifice.

Thus, according to Marshall, the "effort" of working and the "sacrifice" of waiting are the elements that ultimately provide value and price to objects. If the cost is expressed as disutility, then it can be balanced by the utility of demand. As a result, for the first time, an adequate interpretation of the equilibrium price through the forces of demand and supply was given, since both of these forces could be evaluated through utility (positive or negative). This scenery can be illustrated by a graph devised by Marshall and which will become another of his trademarks: the "cross" of supply and demand, which represents the bid price (increasing) and the ask price (decreasing) to each quantity, such as those that appear in Graph No 1.

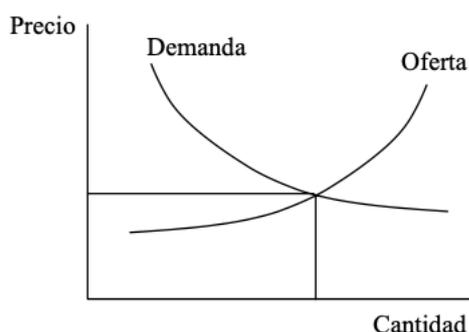


FIGURE 1. MARSHALL'S GRAPHICAL REPRESENTATION OF THE SUPPLY AND DEMAND CURVES

For Marshallian, the price of all products and all factors (wage/capital) was such that the respective markets always tended to an equilibrium position. Now, in equilibrium, supply equals demand, which means that the entire mass of the products and all the factors offered can be placed on the market. This means, in turn, that anyone who wants to sell their products or services at the prevailing equilibrium price can effectively do so.

Among the premises of the neoclassical theory is that there is an automatic and magnetic tendency that pushes the system to equilibrium and does not rest until it reaches that state. This tendency to the equilibrium in all the markets of the economy is known as Say's law of markets. Jean Baptiste Say (1767–1832) expressed an idea that was based on the principle that all individuals are both producers and consumers, since each producer intends to spend the surplus of his product on the purchase of other products. Thus, the production of each producer is essentially the demand for the products of other producers. Say's law appears quite frequently under the catch-phrase '*supply creates its own demand*'. Thus, equilibrium is synonymous with full employment. In this way, full employment becomes a true premise of classical theory as we shall see below.

The creation of a labour market

It is natural that Marshall, by relying on a theory of production costs, was forced to advance more decisively than the early Marginalists in the study of the laws of distribution, since prices of the factor of production become a central element of his value theory.

Marshall's solutions were based on his general idea that all prices are the result of the reciprocal action of supply and demand. Therefore, Marshall creates two different markets to solve the issue, the labour

market and the capital market, which operate in the image and similarity of the market of any other good.

In the labour market, the labour supply curve is upward sloping. This answers to the idea that the workers will offer more work the higher the salary, since for them working one hour more constitutes an increasing sacrifice, which is only compensated by the payment of a higher salary. The supply curve then meets the points where the wage equals the marginal "disutility" of working. In other words the supply curve is the representation of the decision made by workers between the utility reported by the salary obtained for their work versus that provided by the leisure to which they can dedicate their time if they don't dedicate it to work. Furthermore, the labour supply curve of the economy as a whole will not be more than the result of the simple aggregation of those of all workers.

The labour demand curve of entrepreneurs, on the other hand, has a negative slope because Marshall applies here the law of diminishing returns to the employment of all productive agents equally. The idea behind it is that the additional produced product is lesser as occupancy increases. The demand has then a negative slope and shows the points where the wage is equal to the productivity of labour. In equilibrium, the supply of labour is always equal to the demand for labour, and together determine the wage for which both the disutility of labour and the productivity of labour, are equal.

By considering labour as a pure commodity to be analysed in market terms of equilibrium as any other commodity, the problem of distribution was then formulated as a mathematic equation and stopped being on "social contingency". This change in approach resulted in three important new hypotheses:

- a) Labour is a commodity and the amount in which it will be hired depends, as in other cases, on the supply and demand that exists for it in the market.
- b) The labour market is, or should be achieved, under the conditions of perfect competition.
- c) The functioning of the labour market under these conditions automatically leads to full employment of the labour factor at the point corresponding to the wage that balances supply and demand for it.

For Marshall, as long as the system is in equilibrium, there will be full employment. Moreover, his theory presupposes that there is an automatic and magnetic tendency that pushes the system and does not rest until it reaches that equilibrium state. Thus, equilibrium is synonymous with full employment.

The neoclassical understanding of unemployment

With the above general conditions, a completely decentralised decision-making process and an institutional framework of total flexibility that allows wages to rise or fall without restrictions will guarantee the achievement of full employment. And this situation will remain constant as long as the structural conditions of the economy, including general levels of productivity, do not change. A conclusion of this nature had and has, even at the intuitive level, obvious theoretical and normative implications:

- a) The existence of a real equilibrium wage above which it is not possible, at the microeconomic level, for an individual to find employment and, at the macroeconomic level, for the employed population to increase.

- b) Attempts to increase the demand for labour by other means that do not reduce wages will be doomed to failure.

- c) The existence of an unemployed population can only be the result of workers voluntarily refusing to be employed at lower wages. Unemployment is always voluntary and therefore there is no room for permanent situations of massive unemployment.

Following Marshall's theory, unemployment is essentially a phenomenon that belongs to the labour market, because unemployment is by definition an excess labour supply, or in other words unemployment is a transitory disequilibrium state. The Marshallian theory of wages and unemployment predicts, however, that wages will fall to equilibrium, thus ending unemployment. From this it follows that unemployment can only be perpetuated if there is some obstacle that prevents the reduction of wages. It is not at all surprising that orthodoxy, relying on this explanation, has blamed for unemployment the workers unions that refused to see their wages reduced and the labour legislation that also placed limits on wage reductions. In short, only when the wage is "rigid", that is, when some extra-economic factor prevents it from being freely reduced, can unemployment be long-lasting.

Keynes

Historical background

The outbreak of the First World War ushered in what Hobsbawm rightly called the "age of catastrophes." The world had not yet recovered from the trauma of the war when on October 29, 1929, the stock market crash on Wall Street, known hereinafter as "Black Thursday", became the reference for the beginning of the longest depression of the world history of modern capitalism, which is renamed, in its own right, the "Great Depression." In the eight years from 1930 to 1938, the unemployment rate in the United States averaged 26%, in Germany 22%, and in the United Kingdom 15%. Strictly speaking, the recovery of production and employment would come much later and in circumstances that were not too pleasant, linked to the gigantic process of rearmament of the powers. Thus, the Second World War that broke out in 1939 and claimed more than 60 million lives was one of the main sources for industrial reactivation after the crisis of the 1930s.

In the field of economic theory, the Marginalist school in its Marshallian version, the Neoclassics, achieved hegemony, with the help of the so-called second generation of a legion of economists whose presence was felt in the major centres of world powers. The period during which John Maynard Keynes (1883-1946) developed his theoretical production was plagued, as can be seen, with great novelties in the field of economic debates, which lagged behind historical events. One of the major debates was associated with the problem of massive and prolonged unemployment during the Great Depression.

Thus, during the interwar period, a considerable number of economists expressed their dissatisfaction with the traditional theory since the Neoclassical theoretical system failed to account for the causes of inflation, deflation and unemployment, that is, it did not have answers to the dilemmas of the time. Keynes was part of this broad movement, but among all the theoretical efforts that were made, it was his *General Theory of Occupation, Interest and Money* of 1936, the work that managed to break with orthodox thought in the most influential way. In short, Keynes' claims pointed to the historical assumptions and premises on which the theoretical edifice of Neoclassics had been erected, which no longer corresponded to the new economic reality due to the profound transformations that had taken place at the beginning of the 20th century.

Keynes' critics to the (neo)classics

It is necessary to make a clarification, apparently purely terminological, which is in fact loaded with a deep theoretical content. Keynes intends to escape the old and anachronistic theories, but to which economists is his criticism specifically directed? In *The General Theory* he uses various expressions to designate his opponents: "orthodoxy", "traditional theory" or also, especially, "classical theory" or "classical economists". We already know that Keynes was opposed, first of all, to Marshall who was Keynes' professor and mentor. More specifically, Keynes calls "classics" a group of economists made up of both the classics and the Marshallian-Marginalists.

What are the main criticisms that Keynes addresses to Marshall and "the Classics"?

Synthetically, his argument is as follows: the classical system has lost its prestige, fallen into disgrace, so that it must be replaced by a different one. Keynes argued that the most important errors are in the field of the premises, mainly:

- a) the separation between the theory of value and the theory of money, a separation that carries strong conceptual contradictions;
- b) the postulate according to which the economy is always in conditions of full employment;
- c) unconditional adherence to Say's law, which through the labour market, the capital market and the goods market ensures that the economic system moves towards equilibrium in all markets and, therefore, towards full use of available resources.

As we have seen, classical theory presupposes that the economy is always in a state of equilibrium and full occupation, that is, that all the goods and resources that are offered can be placed on the market. For classical theory, then, unemployment is synonymous with disequilibrium. Unemployment should simply be considered an “excess supply of labour”, an imbalance that occurs every time the real wage is above the level corresponding to equilibrium. The causes of unemployment are inexorably associated with the obstacles and difficulties that occur in any market that cause “rigidities” in the adjustment of wages; obstacles outside of economic reign, such as labour unions, laws, and the State. Unemployment is, for the (neo)classics, eminently “voluntary”.

Keynes' General Theory, in contrast, tries to show that the system has multiple possible positions of equilibrium and not a single one that coincides with full employment. In other words, unemployment could also be a situation of equilibrium that could be stable in time. Keynes offers two strong criticisms to Marshall's labour market theory and its corresponding theory of wages and employment, one empirical in nature and the other theoretical. Both directed to the assumptions that are implicit in the construction of the labour supply curve. For this, Keynes introduced in his analysis the difference between **nominal wages** (wage measured in money) and **real wages** (defined as the nominal wage divided by the general price level).

Empirically, if it were true that the real wage is always determined by the supply of labour, each time there is an increase in prices, it should be observed that a portion of the employed workers abandon their work positions, since the new real wages reduced by the increase in prices, should not now be enough to compensate for the marginal disutility of their work. But this is not the answer that is typically verified in practice since, as a general rule, workers do not leave their jobs en masse when prices rise (in the face of inflation).

Theoretically, the critique of the labour market is of greater importance, since it aims to disrupt the adjustment mechanism towards equilibrium (and full employment) that takes place in the Marginalist conceptual framework. Based on the Marshallian theory of prices, in the face of a labour supply excess in which workers would effectively agree to cut their nominal wages in order to achieve full employment, for example a 10% reduction in all wages in the economy represents a fall in the marginal prime cost of all goods that will be approximately the same proportion. This is, according to the classical (Marshallian) theory of value (we explained above), a proportional reduction in all prices should be expected. Thus, a reduction in the nominal wage is accompanied by a reduction in prices of approximately the same percentage magnitude, for which it follows that the real wage remains fixed at approximately the same level as before the nominal wage reduction by the workers. If the real wage is the same, the supply excess, that is, the volume of unemployment, also remains the same. In Keynes's words:

"If nominal wages change, the classical school should be expected to hold that prices would change in almost the same proportion, leaving the level of real wages and unemployment practically the same as before" (Keynes [1936] 2005: 31).

The conclusion is lapidary: workers can reduce their nominal wages but cannot, even if they wanted to do so, cause a decrease in real wages through these consented reductions in money wages. This argument not only obliges us to reject the accusatory attitude of the marginalists towards the workers, but also entails, in addition, very profound theoretical consequences. Following the Marshallian theory of prices, it must be accepted that it is not in the power of the workers to reduce real wages to the equilibrium level with full employment. Then, it must be concluded that the labour market simply does not have an automatic way to reach a full employment equilibrium.

The conceptual consequences that accompany Keynes' criticism of Marshall's labour market turn out to be devastating, since the labour market is one of the pillars of the Neoclassical theory of distribution and also of the theory of value, as Marshall founded his theory of price on the production costs.

Keynesian new theories

As we have seen, Keynes attacked the idea that unemployment was only voluntary and approached the problem of wages from another point of view that was diametrically opposed. He considered, on the one hand, that nominal wages should be the ones taken into account and not, as the neoclassical model did, the real wages because, according to him, workers act under *monetary illusion*. And, on the other hand, that in no way could it be considered that wages had the degree of flexibility required by the neoclassical model in order to achieve equilibrium situations of full employment.

After rolling out the classical labour market, Keynes was forced to offer new theories about wages and the level of employment, since these two variables had remained without explanation after his criticism. He starts by the analysis of the *aggregate demand*. In his *The General Theory*, aggregate demand is not "subordinated" to the volume of supply (as the classic state under the Say's law), but rather other factors govern its behaviour. Aggregate demand is a completely different function that depends on other factors that can be modified in the short term to determine the equilibrium occupancy level. First, Keynes identified two components into which global demand is divided: consumer demand and investment demand. It is necessary to differentiate them because the laws that govern consumption and investment are different, and therefore must be studied separately.

Precisely, one of the main theoretical disruptions in Keynes' theory was understanding of the forces that govern demand dynamics. In his vision, the variations in consumption caused by the increase in income are always less than proportional to the changes in income, since there is a "psychological law" according to which "*when income increases, consumption grows, but not as much as income*". Keynes calls this psychological law that governs consumer spending *propensity to consume*. By stating this, the transmission mechanism that was ensured by Say's law is again broken. According to Say's law, any increase in employment and production produced a rise in income and this in turn was channelled to demand. Now, according to Keynes, any time employment, production and therefore income grows, it can only be assured that consumer demand will increase less than the original increase in income.

Keynes' reasoning is simple: *consumption demand* is not enough to exhaust the increases in output, so, to reach equilibrium it will be always necessary a certain volume of *investment demand* that covers the difference. However, investment demand does not depend on changes in production; so such an increase is not assured. Therefore, two fundamental consequences can be deduced in Keynes's system:

- a) the magnitude of investment demand is the one that “rules the game”, because once its level is determined, the corresponding equilibrium level of employment can be obtained;
- b) if investment demand is small and insufficient, the equilibrium occupation volume may well be below that required to guarantee full employment. Hence, full employment is not the only state of equilibrium and towards which the economic system necessarily tends, as the classical system used to say.

The full employment situation is a special case that is only realised when the propensity to consume and the incentive to invest are in a mutual relationship. Investment must always “fill the gap” between the cost of any level of production (global supply) and consumer demand, always lower. As can be seen, unemployment could be then a situation of equilibrium. The global supply is determined by the technical conditions of production (the costs associated with each level of employment) and, in the short term, must be considered fixed.

It can also be concluded that from this explanation there is a shift with respect to the classical interpretation of unemployment, the identification of its “responsible” and the appropriate remedies to get the economy out of that state. Indeed, for Marshall unemployment was mainly due to the resistance of the workers (generally protected by a permissive state), who refused to reduce their real wages until reaching equilibrium with full employment. The image projected by Keynes's system is very different. Now, the main cause of unemployment becomes weak demand; more precisely, weak investment demand. Very far from the spirit of orthodoxy, the responsibility for unemployment falls on the backs of those who establish the volume of investment, that is, of the businessmen. The State, for its part, instead of appearing in the dock by preventing the proper functioning of the markets, now becomes an alternative source of demand, which comes to complement or replace the declining impulse of the entrepreneurs who invest less than enough to provide full employment. It can now be understood why *The General Theory* became an antidote to the stale medicine of classical orthodoxy that, in the face of unemployment, recommends reducing wages, reducing public spending, and making labour legislation more flexible.

To sum up, the political consequences of Keynes’s thesis clearly differ from the Neoclassical and are well known:

- a) There may be equilibrium situations that imply unemployment.
- b) Unemployment could be involuntary due to downward wage rigidity
- c) Increasing employment in unemployed situations can be achieved by increasing induced incentives in investment demand, which means that exogenous market interventions are not negative, but are essential to achieve full employment.

The New Models

History strikes back

Over time, the Keynesian theses acquired great influence thanks to the fact that they immediately showed much greater capacity than the Neoclassical ones to deal with the economic phenomena of the time. However, none of the successive updates to the original Keynesian model provided sufficiently powerful answers, theoretically and politically, to the problems that emerged throughout the 1970s and 1980s.

Keynesian policies had provided satisfactory solutions during the expansionary growth years of the postwar period, but they would become truly ineffective in the face of a new type of recession of the last decades of the 20th century. The combination of high levels of unemployment brought into question the Keynesian use of economic policies. The internationalisation of economic relations collided with the analysis of demand in closed economies. The productivity crisis that forced the technological reconversion and the surge of a very deep distributive conflict that made it impossible to approach employment regulation as one more dimension of income policy, were obstacles that the original Keynesianism was not in conditions to solve. As happened to the Neoclassical model, reality also took a heavy toll on the Keynesian school of thought.

Friedman's return to (neo)classic

In the 1970s, high rates of inflation and unemployment appeared simultaneously. This necessarily resulted in an alteration of the bases of understanding of the phenomenon of unemployment and, with it, of the theoretical explanation of the functioning of the labour market. At the macroeconomic level, this explanation was transferred to the concept of the "*natural unemployment rate*" initially developed by Milton Friedman (1968), founder of the **monetarist school** whose main ideas stated the rejection of the basic relationships of the Keynesian model.

In the new economic conjuncture, **stagflation** (persistent high inflation combined with high unemployment and stagnant demand), became the new dominant paradigm. Friedman returned to the more radical implications of the Neoclassical model about the limited viability of expansionary demand policies (State's incentives to investment demand) to reduce unemployment below its equilibrium level beyond the short term. The existing unemployment rate will be the natural unemployment rate and the economy will always find itself in a general equilibrium situation of full employment. Understanding, again, that this effective unemployment rate, which does not necessarily have to be zero, will correspond to voluntary unemployment.

In reality, the concept of the natural rate of unemployment is just a renewed version of the neoclassical idea that there are certain equilibrium levels of real wages and employment in the economy that cannot be altered through alterations in prices. The normative proposition that derives from this is evident: to achieve increases in the level of employment it is only possible to act by reducing the wages of the workers.

Neoclassics' school revisited: the theory of human capital

With the progressive return of Neoclassical theory, there is an intense and parallel revision of its approaches to the labour market, whose limitations become more and more evident when confronted with reality. The lack of homogeneity both in the labour supply, that is, in the qualification of workers, and in the labour demand led to the elaboration of what can be considered as the main contribution of the Neoclassical school to labour economics: the theory of human capital.

This theory suggests that the heterogeneity of workers is the result of the different degrees of investment that they make in their training and qualifications improvement. Heterogeneity is, therefore, the result of an investment process: investment in human capital. The analysis is posed from the beginning, in the field of individual decisions, based on the hypothesis that the subjects have the capacity to choose both the amount of work they are willing to offer and the quality of that work, which will depend on their prior decision to invest in a specific type of training.

This revision leaves aside the traditional neoclassical conception of labour as a commodity without other specific connotations beyond being carried out by human beings, as Alfred Marshall would argue. The striking difference and the new neoclassic "miracle" is how on their journey back to the origins, this theory managed to make labour disappear, even as a commodity, turning it into capital.

In any case, unemployment comes to be understood as something that originated and resolved in the field of individual decisions, it is a specific problem for each subject, and not a social problem. The diagnosis of unemployment involves mainly insufficient or inappropriate investment in training, and therefore the regulatory proposals in this analysis refer to the field of educational policies rather than to those of the labour market.

Institutionalism and new Marxism

Following the logic that runs through all Neoclassical variants, institutions and regulations are nothing more than rigidities that keep markets away from perfect competition and cause situations in which the real wage is excessively high compared to the other conditions of the product and labour markets.

Confronting these ideas, the institutionalist current aims precisely at highlighting the importance of social and institutional influences on the behaviour of agents and, therefore, on the evolution of wages, employment and unemployment. Unlike what happens in the neoclassical model, this currently considers institutions as endogenous variables. From a much more descriptive than analytical perspective, the institutionalist authors consider that the forms of industrial organisation, the existing conditions in the goods market, the available technology, the strategies of business control or labour market regulations, play a determining role on the structure of that market. A market that, on the other hand, is neither unique nor competitive in nature, but rather has a fragmented and imperfect structure.

The labour market would thus be made up of various non-competitive segments and with differences in their remuneration levels and working conditions as a consequence of their "dual" nature and not only of the different levels of education and training of workers. According to this "dual" vision, the functioning of the labour market could be explained starting from the idea that it is divided into two large segments: the primary market (which would encompass the good jobs in the market, that is, those with high salaries, stability, opportunities for employment advancement, among others) and

the secondary market (jobs with low wages, instability, few opportunities for advancement, and so on) would be confined.

This theory is based on the idea that a series of social factors and, especially, demand factors, had caused, over time, a dualization of the labour market. At the same time the relationship between education and work is governed by this duality, where the institutional structures that are more or less stable over time (for example, barriers to access to the university, or the socio-cultural profile of the student, or family influence at the time of choosing the race) also condition the labour supply side. In short, this theory assumes that society is institutionally structured, that is, conditioned by habits and rules that govern the production and distribution of wealth.

Along with institutionalist theories, another set of different theories that derived with unequal fidelity from original Marxism, constituted the other alternative to (new)Neoclassicals. The fundamental point of confrontation between Marxist and neoclassical theories is the distinction between the concepts of labour as a commodity that is bought and sold in the market (neoclassic); and the concept of labour as a factor of production that is incorporated into the production process (Marxist).

Now, from the original Marxist approach, centred on the aforementioned distinction, different readings on labour and the dynamics that govern it have been drafted by neoMarxism. All of them agree, however, that in order to detect the determinants of the volume of employment or unemployment in an economy and the guidelines and rules that govern the distribution of income within it, contextual factors must be analysed and not only those that given in the markets: the specific working conditions, the hierarchy inherent in wage labour, the control mechanisms articulated to convert labour power into effective labour and, in general, the general conditions of the capitalist economy at a given moment. In short, labour relationships are not only a market relationship but a social relationship.

Feminist economics

Feminist economics is one of the current movements for pluralism in economics that has been acknowledged by the mainstream of the profession. It highlights issues which affect women that have not traditionally been recognised in a field dominated by men. Moreover, it seeks to carve out a space for women in the discipline, for fairness and diversity reasons and because it means that women's issues are more likely to be considered. This theory rightfully argues that economic theory presents an historical male-centred bias.

Feminist economists argue that women perform a lot of labour which goes unpaid and unnoticed but which keeps the economy, society, and individual families afloat. Unremunerated household work is not considered present in the labour market, plus the gendered expectations which push women into certain tasks and occupations, has historically put women in positions which have not been rewarded as much as men's work both socially and financially. Furthermore, unpaid labour doesn't stop at home, though. The 'emotional labour' performed by women at work as women are expected to do less important, menial tasks that do not advance their careers but are necessary to keep the workplace going. These range from literally doing the housework in the office – keeping the place tidy, bringing in food – to taking minutes, supporting others, creating schedules and the like.

Women have historically performed large amounts of labour which is rendered invisible by social and financial conventions, and economic theories and schools have failed to recognise this. Better data

and an incorporation of these concepts into economists' and society's ideas of 'labour' would be a huge step forward.⁵

Ecological economics

Neither classical, neoclassical, Marxist or Keynesian schools of economy have acknowledged the problem of economic scale. All of them have always valorized economic growth, as at the time they were developed environmental problems were not of real concern. Ecological economics' most important contribution is the argument that the human economy is a subsystem of the finite earth's natural life-support system. Implied in this argument is a new metric of economic health, the life-value rather than the money-value of that which economies produce and distribute.

In recent decades we have understood that climate change and air pollution are major environmental issues which affect us all. The main tension point is that although regulations like green energy policies can lead to notable environmental improvements and health benefits, they also impose additional production costs on firms, especially in sectors exposed to trade and intensive in labour and energy.

However, ecological economics schools argue that the benefits of such environmental regulations are likely to outweigh any costs. Green growth policies aim at improving environmental quality and economic growth at the same time. A successful transition towards green growth can create new opportunities for workers, as job creation can be achieved in a number of economic sectors with low emission intensities, while job destruction occurs in emission-intensive sectors.

Most probably in most countries, job reduction in the central scenario will affect 'Blue collar and farm workers' the most. This job category is largely employed in energy sectors and energy-intensive industries, which are the most impacted sectors. Workers in the categories 'Service and sales' and 'Managers and officials' generally benefit most in terms of wage income, since these job categories are more represented in sectors that are the least affected by the policy (such as services).

The success of green growth policies depends on the capacity of the firms and workers to adapt to the changes in economic structures induced by the policies. Further knowledge of the job categories that are most vulnerable when implementing green growth policies is fundamental to adjust education and training policies, as well as redistributive schemes that will accommodate the green growth objectives.

⁵ Our project contains an entire chapter on feminist economics, so we strongly recommend you check it for further information on these theories.

Conclusions

New context, same orthodoxy spirit

In order to globally assess the changes in approach that have been taking place in the economic theory and especially with regards to labour and employment theories, it is important to bear in mind the conflictive social environment in which they have taken place. In fact, history has shown that paradigm shifts always occur alongside important economic transformations derived from the different interests of different social groups and to which economic analysis can never be and has never been alienated from.

In recent years there have been very important transformations in the nature and organisation of labour and also in the general economic conditions that influence it: the technological base has been modified almost radically, the nature of the financial systems and their relationship with the real economy have changed, a new system of rights appropriation and different regimes for the use and mobility of resources have been established. The regulatory system and other institutions, conventions, and social values that structure society and economic relations in general have changed. Regarding work, the conditions for training the supply and demand for work have changed, the age pyramids, the composition of the active and inactive population, working times, levels and conditions of training, all of which have also changed.

All these changes are the result of various factors whose specific combination is different in each territory depending on the social conflict originated, and the degree of success or failure occurred from previous models of regulation and intervention. But what characterises the currently dominant approaches is not precisely the recognition of these differences but rather a view of a generality with which their main political-economic postulates are assumed.

The basic "consensus" that today dominates economic thought, or in other words the current orthodoxy is under the ideas of the "Washington consensus" a model that prescribed to the countries of the periphery a series of proposals that state what the greatest economic and political powers see that they need to be economically acceptable. These proposals are embodied in a series of postulates that constitute the essential referents of the Neoliberal doctrine:

- 1) The need to reduce the distorting intervention of the government as much as possible
- 2) Price stability should be the central objective of macro policies
- 3) The main task of the government must now be to make markets function as freely as possible, without regulatory constraints.

In the unique case of Europe, this consensus has also materialised in another relevant aspect from the point of view of work and employment. Since the monetary union is built with great limitations to the mobility of labour for very diverse reasons, the balance must be achieved through the flexibility of prices and wages, which has led to the strengthening of flexibility strategies, especially in the labour market, to promote competitive tax strategies and the progressive dismantling of the Welfare State.

The Theoretical Approach of the New Orthodoxy in Labour Economics

As we have shown, contemporary approaches have developed in different lines and magnitudes. Nevertheless, what can be understood as today's orthodoxy presents characteristics that have found global consensus regarding the instruments that should govern labour. The main ideas are:

- 1) employment or unemployment problems have more to do with the existence of inadequate individual strategies than with aggregate (social-collective) problems,
- 2) introduction of an ideological structure that makes labour disappear as a productive factor and transforms it into a specific type of capital and workers into capitalists. In this way, labour becomes capital in the purest neoclassical sense and the class conflict disappear,
- 3) that the level of employment is a constant and not a variable on which it is necessary to try to influence through the instruments of macroeconomic regulation. On the contrary, the level of employment (and therefore, unemployment) is given by the natural rate. The unemployment problem is once again seen as voluntary.

A final characteristic of the new orthodoxy is that it has acquired extraordinary political influence without its adherents having found the minimum empirical evidence that they should have to be considered scientific. It has not been possible to demonstrate that greater flexibility in labour reforms are effective instruments to influence the level of employment. Nor can it be demonstrated that increased influence from labour unions is the cause of unemployment, as the academic orthodoxy repeatedly points out or that which is pronounced by institutions such as the International Monetary Fund.

Considering all the above, it is urgent to question: to what extent does it make sense for the economy to ignore the problem of the effective welfare of workers or of society in general when it addresses the problem of unemployment? When the International Labour Organisation points out that in 2019 the lowest 20 percent of income earners – around 650 million workers – earn less than 1 percent of global labour income⁶, and that currently we are reaching the highest unemployment rate of the last 30 years one should wonder: is it reasonable to maintain that this situation occurs simply because such workers have decided not to invest enough in themselves or that they are voluntarily unemployed because they insist on not accepting lower wages?

In short, the final balance about the knowledge that different schools of economics have added to the study of work and employment is quite frustrating. As we have seen, current dominant analyses prevent us from contemplating the necessarily more global-social nature of the unemployment problem. These limitations are precisely those that indicate, in turn, the great challenges that economic analysis faces in order to understand and explain the problems of labour. Challenges that definitely will be aggravated by the current health global crisis that started in 2020 and that is already showing main changes in the labour structures and organisation.

⁶ Access: https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_712234/lang--en/index.htm And <https://data.worldbank.org/indicator/SL.UEM.TOTL.ZS>

References

- Mario E. Bergara, Nora Berretta, & Umberto DellaMea Palumbo (eds.) (1999) *Economía para no economistas*. Montevideo, Dep. de Economía, Fac. de Ciencias Sociales, Univ. de la República.
- Keynes, J.M. (1996) *The collected writings of John Maynard Keynes. 7: The general theory of employment interest and money*. Repr. London, Macmillan.
- Kicillof, A. (2010) *De Smith a Keynes: siete lecciones de historia del pensamiento económico ; un análisis de los textos originales*. Temas de economía. Buenos Aires, Eudeba.
- Marx, K., Scaron, P. & Marx, K. (20) *El capital: crítica de la economía política*. Biblioteca del pensamiento socialista Série Los clásicos. México Madrid, España, Siglo Veintiuno Ed.
- OECD, (2017), *Working Party on Integrating Environmental and Economic Policies*.
- Pacífico, A., Trucco, I., y Barletta, M. A. (2014) El mercado de trabajo y la educación: la visión neoclásica e institucionalista. *Revis- ta Ciencias Económicas*.
- Sapsford, D. & Tzannatos, Z. (1997) *The economics of the labour market*. Macmillan texts in economics. 2. print. Basingstoke, Macmillan.
- Smith, A. & Skinner, A.S. (1970) *The wealth of nations: Books I-III*. The Pelican classics. Harmondsworth, Penguin.
- Torres López, J. (2015) *Economía política (5a. ed.)*. [Online]. Madrid, Larousse - Ediciones Pirámide. Available from: <http://public.ebookcentral.proquest.com/choice/publicfullrecord.aspx?p=4626685> [Accessed: 19 May 2020].
- Torres López, Juan Montero Soler, Antonio (2005) Trabajo, empleo y desempleo en la teoría económica. *Principios. estudios de economía política*. (3), 5–36.
- Tsoufidis, L. (2010) *Competing schools of economic thought*. Berlin ; London, Springer.

3. Training material

Activity 1: Bingo!

Overview

The activity is designed for students to internalise the main characteristics of the different schools of economic thought.

Aims

- to stimulate thinking about the theoretical concepts explained
- to explore the main differences between the different economic systems
- to provide some basic facts about the Classic, Marginalist, Neoclassic, Marxist and Keynesian models

Materials and time

The bingo is designed as a Table as shown below, that could be printed in advance or be drawn manually by the instructor and the students. Time can be adjusted from 30 minutes to an hour.

Group size

10 minimum

Instructions for trainers

1. Break up the class into small groups.
2. The teacher draws/distributes the following empty table, explaining that the team that completes 3 X in a vertical column first should shout BINGO!

	Classics (without Marx)	Marginalis t	Neoclassic	Marxist	Keynesia n
The first school that placed economics as a science					
For this school the state should not intervene					
Founder of the Welfare State					
Strongest critic of capital concentration					
Invented the concept of the invisible hand					
Defined the concept of abstract labour and surplus					
Based in value theories					
Invented the labour market model					
Invented the Utility theory					
For this theory full employment is not guaranteed by market laws					

Table with results (for the instructor)

Theories/Schools	Classics (without Marx)	Marginalis t	Neoclassics	Marxist	Keynesia n
The first school that placed economics as a science	X				
For this school the state should not intervene	X	X	X		
Founder of the Welfare State					X
Strongest critic of capital concentration				X	
Invented the concept of the invisible hand	X				
Defined the concept of abstract labour and surplus				X	
Based in value theories	X	X		X	
Invented the labour market model			X		
Invented the Utility theory		X			
For this theory full employment is not guaranteed by market laws					X

3. After the first team shouts Bingo! The instructor must check that the answers are correct and facilitate a dialogue with the students in case of any questions.

4. If the first team answered all points correctly, the exercise would end there. Otherwise, the instructor will continue reading out the topics that remain on the table.

Activity 2: Quiz of value

Overview

The activity is designed for students to understand the differences between the theories of value explained in this chapter. As the concepts may be confusing, it is suggested to give a brief recap of specifically this topic before the quiz.

Aims

- to solidify the concepts explained around the theories of value and its connection with labour

Materials and time

No materials are needed. We suggest you use an online platform like myquiz.org (for free up to 25 students). Time can be adjusted from 30 minutes to an hour.

Group size

Individually

Instructions for trainers

1. The trainers should provide the students with the link of the quiz that should be prepared in advance.
2. The instructor reads out the questions for each round (see Quiz Questions below) and can pause the activities if students have any questions.
3. After finishing the quiz, the instructor can see who is the winner and provide the student with a prize (it can be symbolic!) . In total, this part of the activity should take between 20 to 30 minutes.

Questions

1. The first author to associate the value of commodities with labour is:
 - a. Marx
 - b. Adam Smith
 - c. David Ricardo
2. For Ricardo, the primary regulator of prices is:
 - a. The labour time to produce a commodity
 - b. The exchange value
 - c. The wages of the employees
3. Ricardo's main addition to Smith's value theory is:
 - a. A better determination of the 'labour time'
 - b. That wages are like the price of any other merchandise, and are subject to permanent variations
 - c. An update of the 'primitive society'
4. Despite their differences, Smith and Ricardo agreed that:
 - a. Commodities are exchange when the demand and offer price coincide
 - b. That the addition of wages and benefits conform prices
 - c. That only and exclusively labour has the capacity to "create" value

5. The crucial differences between the classics and Marx in the value theories are:
 - a. The difference between abstract labour and concrete labour
 - b. That value and exchange value are not the same
 - c. Both of the above
6. According to Marx 'the magnitude of the value of a commodity changes directly to the quantity of labour and inversely to the productive capacity of the labour invested in it'
 - a. True
 - b. False
7. Marx's socially 'the necessary labour time constitutes the regulator of prices and profit' is analogous to Smith's
 - a. Price theory
 - b. Invisible hand theory
 - c. Both of the above
8. Marx defined surplus value as...
 - a. The difference between total labour time and that required to reproduce the workers' capacity to work
 - b. The difference between unpaid labour and surplus labour
 - c. Neither of the above
9. The school that came to replace *labour value theory* with *utility theory* was:
 - a. Neoclassics
 - b. Keynesian
 - c. Marginalist
10. The main reason why *labour value theory* was abandoned was:
 - a. To differentiate from Marxism
 - b. It was attracting discontent from the establishment as it was leading to 'dangerous conclusions' around issues of social redistribution
 - c. Both of the above
11. For the Marginalist school, the value of a commodity is determined by its utility that refers to the satisfaction that drives from the consumption of a good. True or false?
 - a. True
 - b. False
12. Marshall's main contribution to theory of value is:
 - a. The idea of marginal utility
 - b. The ideas of *sacrifice of labour and the sacrifice of waiting*
 - c. The dismissed of a law of value

Alternative note: if the instructor considers the exercise too difficult for the audience, it is suggested that instead of using the online MyQuiz tool, to facilitate it as an offline exercise (as it is basically a single choice exercise). In this case, the students won't be pressured by the online tool timing and could have next to them the information provided in this chapter to search for the answers in it.

Activity 3: True or false

Overview & Aims

The activity is designed for students to understand the differences between the theories of the Neoclassical school and Keynesian school.

Materials and time

The instructor is encouraged to write out the statements on a blackboard or in a PPT presentation in order for the students to have them visible during the whole exercise.

Group size

It could be carried out either in groups or individually. The activity could take 20/30 mins and it is ideally followed by a discussion.

Instructions for trainers

1. According to the number of people the instructor should decide how to divide the group.
2. The instructor presents the statements to be defined as true or false to the students and gives them 15 minutes for them to think/discuss in groups.
3. In the end each group shared their results, justifying only the False statements.
4. The instructor could decide to either reveal the result for each statement at the time or at the end of the exercise. Again, in any case, a discussion is encouraged.
5. The instructor can select from the following list the number of T/F to analyse according to the time the group has, and how difficult they found it.

Statements

1. In neoclassical theory, there is an automatic and magnetic tendency that pushes the system to equilibrium and does not rest until it reaches that state (T)
2. The supply curve is the representation of the decision made by workers between the utility reported by the salary obtained for their work versus that provided by the leisure and it has a downward slope (F: first part is true but the curve has an upward slope)
3. In neoclassical theory, the labour market automatically leads to full employment at the wage that balances supply and demand (T).
4. In neoclassical theory, unemployment is voluntary and can be solved by increasing the labour demand (F: first part is true, but it can't be solved by increasing the demand, the only way of solving unemployment for this theory is reducing wages).
5. In neoclassical theory, the economy is always in conditions of full employment and wage rigidity is the cause of unemployment (T)

6. In Keynesian theory, unemployment could also be a situation of equilibrium that could be stable in time, but workers can reduce their wages to come back to equilibrium (F: first part true, second part false: workers cannot reduce unemployment because they can't reduce real wages)
7. Disagreeing with Say's law, in Keynesian theory any increase in the production and income doesn't always increase demand as the latter establishes a distinction between consumption demand and investment demand. (T)
8. In Keynesian theory if investment demand is big, the equilibrium occupation volume may well be below that required to guarantee full employment (F: just the opposite, if the investment demand is small and insufficient it may lead to unemployment)
9. In Keynesian theory, investment must always "fill the gap" between the cost of any level of production (global supply) and consumer demand, always lower (T)
10. In Keynesian theory, the cause of unemployment is a weak demand, more precisely, weak consumption demand (F: it's a weak investment demand)
11. In Keynesian theory, exogenous market interventions (from the state) are not negative, but are essential to achieve full employment (T)

Activity 4: Grouping the groupies

Overview & Aims

The activity aims at connecting the most relevant author and scholars with each school of economic thought explained in this chapter. It also adds the distinction between orthodox and heterodox economic lines for the students to understand the positions of each line of argumentation.

Materials and time

The instructor could either use an online platform like Miro.com to carry out the exercise or do it offline by printing and cutting the forms shared below.

Group size

It could be carried out either in groups or individually. The activity will take 20/30 mins.

Instructions for trainers

1. According to the number of people the instructor should decide how to divide the group or whether to carry out the activity individually.
2. The instructor presents the different schools in an unorganised way (Figure 1) and asks the students to arrange them in an order as they see fit (it could be suggested to follow the historical orientation provided in the chapter). The instructor could ask which schools seem to belong more to an heterodox or an orthodox line of the economy based on students' general knowledge.
3. After the students have arranged the different schools they are then asked to locate the names of the authors around each of the schools to which they belong.
4. As this is an exercise designed to stimulate connections, there are no right or wrong answers. Nevertheless, what's shown in Figure 2 is the closest to what is considered convention. Again, in any case, a discussion is encouraged.

Figures

Figure 1. Unarranged schools

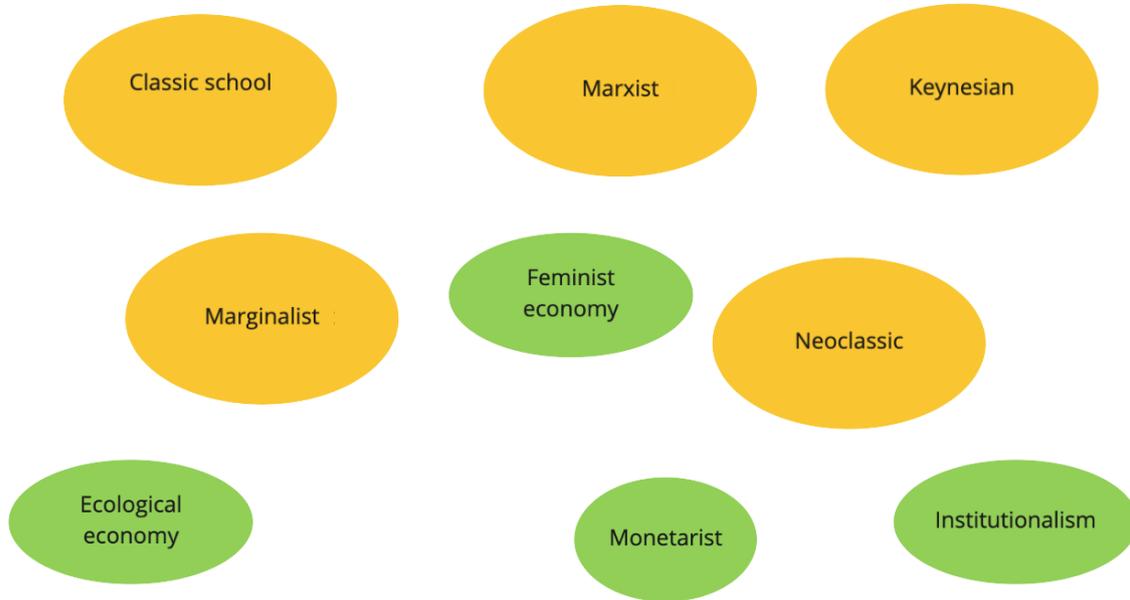
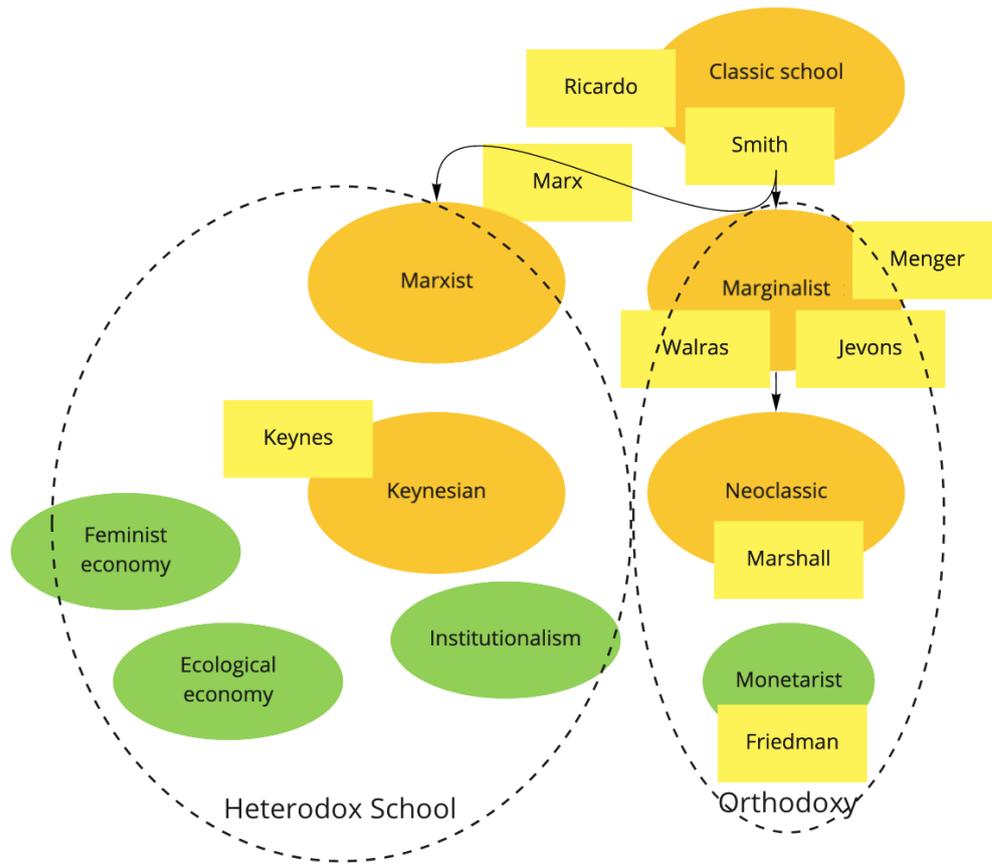
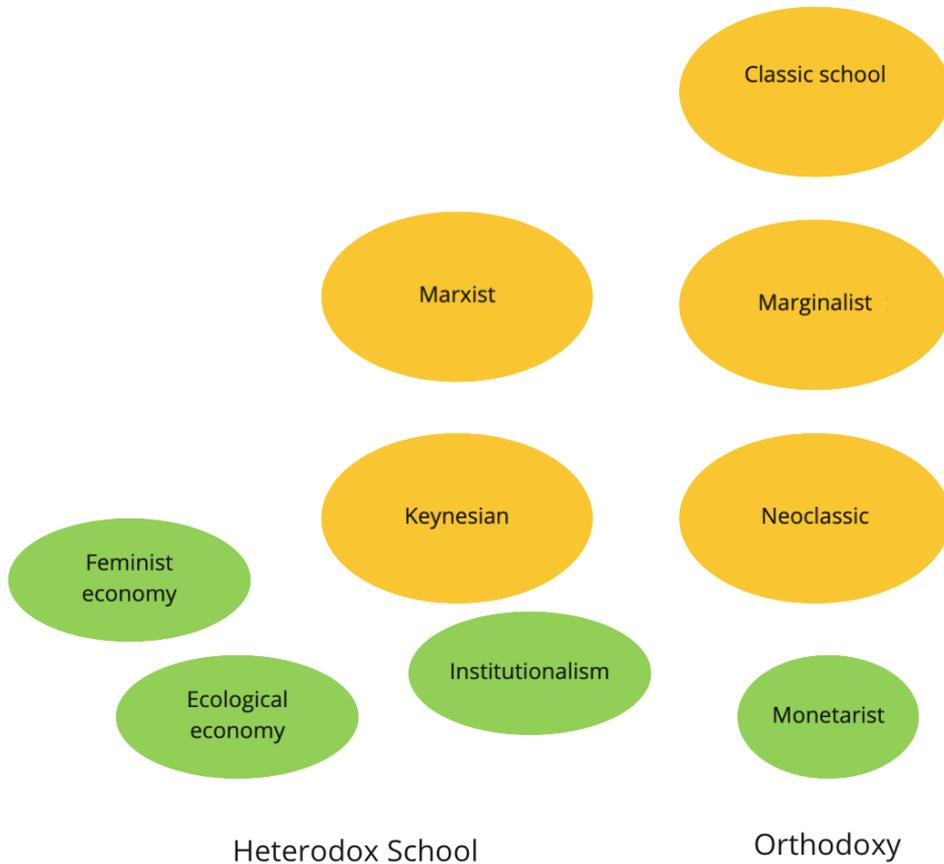
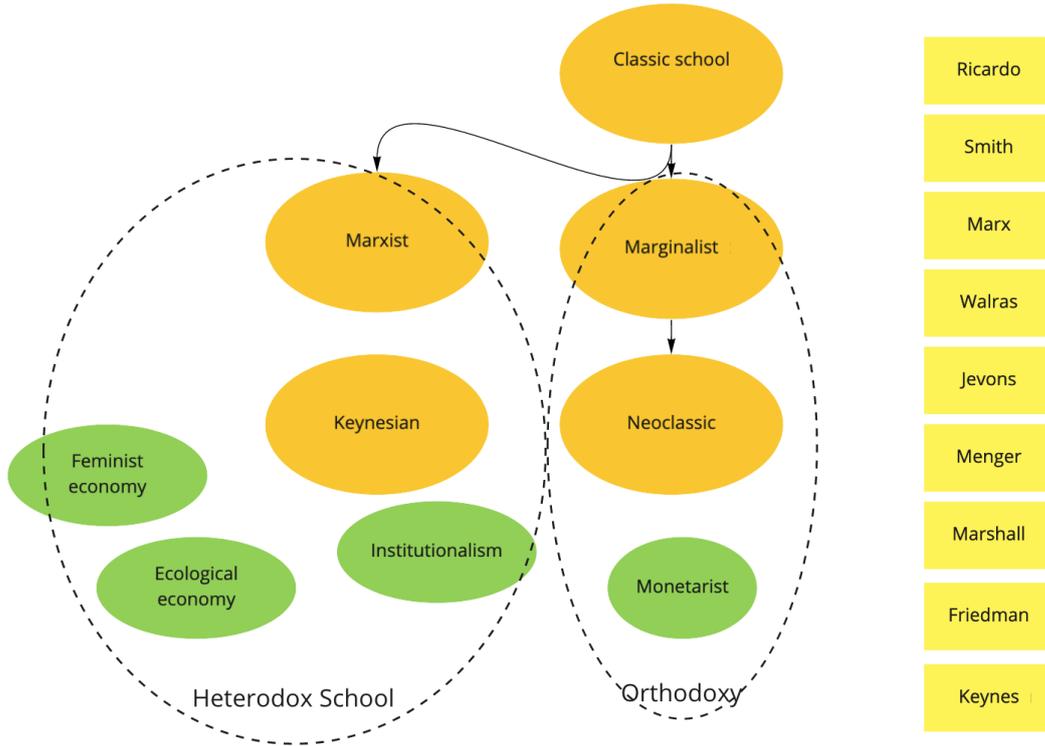


Figure 2. Final result



For the instructor to print:



4. Interactive learning

Activity 1: Quiz of value

Questions

1. The first author to associate the value of commodities with labour is:
 - a. Marx
 - b. Adam Smith
 - c. David Ricardo
2. For Ricardo, the primary regulator of prices is:
 - a. The labour time to produce a commodity
 - b. The exchange value
 - c. The wages of the employees
3. Ricardo's main addition to Smith's value theory is:
 - a. A better determination of the 'labour time'
 - b. That wages are like the price of any other merchandise, and are subject to permanent variations
 - c. An update of the 'primitive society'
4. Despite their differences, Smith and Ricardo agreed that:
 - a. Commodities are exchange when the demand and offer price coincide
 - b. That the addition of wages and benefits conform prices
 - c. That only and exclusively labour has the capacity to "create" value
5. The crucial differences between the classics and Marx in the value theories are:
 - a. The difference between abstract labour and concrete labour
 - b. That value and exchange value are not the same
 - c. Both of the above
6. According to Marx 'the magnitude of the value of a commodity changes directly to the quantity of labour and inversely to the productive capacity of the labour invested in it'
 - a. True
 - b. False
7. Marx's socially 'the necessary labour time constitutes the regulator of prices and profit' is analogous to Smith's
 - a. Price theory
 - b. Invisible hand theory
 - c. Both of the above
8. Marx defined surplus value as...
 - a. The difference between total labour time and that required to reproduce the workers' capacity to work
 - b. The difference between unpaid labour and surplus labour
 - c. Neither of the above

9. The school that came to replace *labour value theory* with *utility theory* was:
 - a. Neoclassics
 - b. Keynesian
 - c. **Marginalist**

10. The main reason why *labour value theory* was abandoned was:
 - a. To differentiate from Marxism
 - b. It was attracting discontent from the establishment as it was leading to 'dangerous conclusions' around issues of social redistribution
 - c. **Both of the above**

11. For the Marginalist school, the value of a commodity is determined by its utility that refers to the satisfaction that drives from the consumption of a good. True or false?
 - a. **True**
 - b. False

12. Marshall's main contribution to theory of value is:
 - a. The idea of marginal utility
 - b. **The ideas of *sacrifice of labour and the sacrifice of waiting***
 - c. The dismissed of a law of value

Alternative note: if the instructor considers the exercise too difficult for the audience, it is suggested to instead of helping by the online MyQuiz tool, to perform it in an analogic way (as it is basically a single choice exercise). In this case, the students won't be rushing under the online tool timing and could have next to them the information provided in this chapter to search for the answers in it.

Activity 2: True or false

Statements

1. In the neoclassical theory there is an automatic and magnetic tendency that pushes the system to equilibrium and does not rest until it reaches that state (T)
2. The supply curve is the representation of the decision made by workers between the utility reported by the salary obtained for their work versus that provided by the leisure and it has a downward sloping (F: first part it's true but the curve has an upward sloping)
3. In the neoclassic theory the labour market automatically leads to full employment at the wage that balances supply and demand (T)
4. In neoclassic unemployment is voluntary and can be solved by increasing the labour demand (F: first part is true, but it can't be solved by increasing the demand, the only way of solving unemployment for this theory is reducing wages)
5. For the neoclassic school the economy is always in conditions of full employment and wage rigidity is the cause of unemployment (T)
6. For Keynes unemployment could also be as a situation of equilibrium that could be stable in time, but workers can reduce their wages to come back to equilibrium (F: first part true, second part false: workers can't reduce unemployment because they can't reduce real wages)
7. Opposing to Say's law, for Keynes any increase in the production and income doesn't 'always increase the demand as the latter establishes a distinction between consumption demand and investment demand. (T)
8. For Keynes investment demand is big, the equilibrium occupation volume may well be below that required to guarantee full employment (F: just the opposite, if the investment demand is small and insufficient it may lead to unemployment)
9. For Keynes . Investment must always "fill the gap" between the cost of any level of production (global supply) and consumer demand, always lower (T)
10. For Keynes cause of unemployment is a weak demand, more precisely, weak consumption demand. (F: a weak investment demand)
11. For Keynes exogenous market interventions (from the state) are not negative, but are essential to achieve full employment (T)