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Thorstein Veblen's Theories of Governmental Failure:

The Critic of Capitalism and Democracy Neglected Some Useful Insights, Hindsight Shows

By CHARLES G. LEATHERS*

ABSTRACT. IN THE THEORY OF BUSINESS ENTERPRISE, *Thorstein Veblen* introduced a general theory of *governmental failure* in constitutional *democracies* based on the *common man's* delusion that *policies* benefiting *businessmen* also benefited him. This general theory runs consistently through Veblen's later works and was developed more fully in THE VESTED INTERESTS AND THE COMMON MAN. But other elements of an *economic* theory of government introduced in THE THEORY OF BUSINESS ENTERPRISE were less durable. A briefly sketched economic theory of *political parties* was never mentioned again in any of Veblen's subsequent writings. A concept of *governmental officials* pursuing their own self-interest did reappear in Veblen's wartime works, but was completely missing in ABSENTEE OWNERSHIP. The concept of a Leviathan-type government which pursued policies detrimental to the interests of both the common man and businessmen was repudiated in THE NATURE OF PEACE. The conditions for its existence had been eroded by the influence of modern *industrial technology* on *military operations*.

ECONOMIC THEORIES of political behavior have become standard components of modern political economy. As exemplified by the new "constitutional economics" (see Mckenzie 1984), several such theories predict that political decisions reached through the democratic processes will fail to promote welfare maximization. In this paper, we examine earlier concepts of governmental failure that appear in the works of Thorstein Veblen on the business enterprise system.

I

Veblen on Government

THE INSTITUTIONAL PROCESSES of democratic political decisionmaking received little attention in Veblen's analyses of the business enterprise system and its attendant leisure class culture. As Rick Tilman has explained:

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Veblen's concern was not with the structural forms and procedural basis of representative government but with a political economy which would maximize the economic welfare of the common man. He placed far more emphasis on maximizing the production and distribution of goods than on the traditional institutional and procedural mechanisms of representative government (1972, p. 316).

But Veblen certainly did not ignore government altogether. Charles Beard credited Veblen with doing the most original work of his time on the economic basis of governmental structure (Dorfman 1966, p. 316).

The basic theme in Veblen's discussions of the public sector in modern industrial democracies was that representative governments tend to implement policies that adversely affect the material welfare of the 90 percent of the population not owning enough wealth to make it count. His analyses of governmental failure attract our attention for several reasons.

First, Veblen's general theory that representative government functions for the benefit of the businessmen contrasts sharply with the modern theories of governmental failure rooted in neoclassical methodology. In the latter, the assumption of rational utility-maximizing individuals is paramount. Political failures occur because political mechanisms fail to channel rational self-interested decisions by individuals into optimal collective decisions. Special interests are able to unduly influence government policy because the democratic processes fail to force an accurate weighing of social costs and benefits in reaching the final decision.

In contrast, Veblen rejected the neoclassical methodology, denying the usefulness of the assumption of rational utility-maximizing individuals in analyzing the true nature of the modern socioeconomic system. (As Rutherford (1984) has noted, Veblen did utilize methodological individualism in his analyses of how businessmen behave. But his broader analyses demonstrated that such rational business behavior failed to contribute to the social welfare.) In Veblen's analyses of government, political failures were predicted because the individuals casting votes in elections were as irrational in their political behavior as in their consumption decisions.

Moreover, Veblen's concept of political failure rested on a different concept of social welfare. The modern political economy approach conceptualizes social welfare in terms of individual utility reflected in market demand prices. Social welfare in the Veblenian context meant maximum production and equitable distribution of serviceable goods (as opposed to vendible ones). Pecuniary (market) values, which can be manipulated through "sabotage," reflect human welfare only in some metaphysical sense that is totally incompatible with the modern world of science and technology.

Second, despite Veblen's rejection of neoclassical methodology, he came

close on several occasions to anticipating certain elements of the modern economic theories of political behavior. In particular, he sketched an economic theory of political parties and hinted that governmental officials may be motivated by their own self-interests. Third, and perhaps most interesting, Veblen presented a second theory of governmental failure in *The Theory of Business Enterprise* (1904) that conflicted with his general theory of governmental failure. This involved a Leviathan-type government that pursued policies actually adverse to the pecuniary profits and long-term survival of businessmen. Curiously, this second theory was effectively repudiated later in *The Nature of Peace* (1919).

II

Governmental Failures in THE THEORY OF BUSINESS ENTERPRISE

THE BASIC FEATURES of Veblen's theories of governmental failures appear in *The Theory of Business Enterprise*. In earlier stages of social evolution, government was an organization that functioned for the control of affairs in the interests of the monarch or dynasty. But under constitutional democracies with parliamentary representation, sovereignty is vested in the great underlying population. Hence, policies of modern democratic governments logically should reflect the collective interests of the "common man." In reality, however, the principal concern of democratic government has become business ends.

A constitutional government is a business government. It is particularly through the expedient of parliamentary voting on the budget that any constitutional executive, *e.g.*, is kept within constitutional bounds; and the budget is voted with a main view of its expediency for business ends. The expediency of business enterprise is not questioned . . . (Veblen 1915, p. 285).

Modern government policies are of a mercantilist nature, *i.e.*, intended to foster trade. But they differ from the older mercantilist policies in one respect.

The modern mercantilism under constitutional rule . . . looks to the prince as a means to the end of commercial gain. With the transition to constitutional rule and methods, the discretion and autonomy in the case has passed from the hands of the prince into those of the businessmen, and the interests of the businessmen have superseded those of the crown.

Representative government means, chiefly, representation of business interests. The government commonly works in the interest of the business men with a fairly consistent singleness of purpose (Veblen 1915, p. 286).

Democratic government functions on behalf of business interests because the "common man", *i.e.*, the general populace, is irrational.

. . . There is a naive, unquestioning persuasion abroad among the body of the people to the effect that, in some occult way, the material interests of the populace coincide with the pecuniary interests of those business men who live within the scope of the same set of government contrivances. This persuasion is an article of popular metaphysics . . . (Veblen 1915, p. 286).

Veblen attributed the common man's irrationality to the influence of atavistic sentiments and institutions. Patriotism, an emotional illusion of being a member of a clan in which benefits are shared in common, was the primary atavistic sentiment involved. The primary atavistic institution involved was property, rooted in the concepts of natural liberty that complied with the commonsense of the 18th century. In the modern period, the common man has become conditioned to accept the legal fiction that pecuniary rights of the businessmen are justified as representing actual contributions to the material welfare of the populace.

. . . The common man is enabled to feel that he has some sort of metaphysical share in the gains which accrue to the businessmen who are citizens of the same "commonwealth;" so that whatever policy furthers the commercial gains of those businessmen whose domicile is within the national boundaries is felt to be beneficial to all the rest of the population (Veblen 1915, p. 289).

To illustrate how business ends are served by democratic governments, Veblen focused on the role of government in international affairs. In the process, he explained that tariffs work to the advantage of the business interests at the expense of the common man. But he also revealed an economic theory of political parties, an image of a Leviathan-type government expanding expenditures to the point that business interests were being adversely affected, and a recognition that personal interests of individuals in governmental positions may influence governmental policies.

III

An Economic Theory of Political Parties

VEBLEN DESCRIBED INTERNATIONAL POLICIES as simply another expression of "business politics" as the machinery and policy of government is utilized to serve the large business interests in international trade and the world market. To provide these business interests with the greatest possible competitive advantage, the forces of the State—legislative, diplomatic, and military—become engaged in a strategic high-stakes game of pecuniary advantage (Veblen 1915, p. 293). In the process, the business interests of each country become joined in a loose organization in the form of a tacit ring or syndicate, operating under a general solidarity against business interests in foreign countries.

The modern political party was described as the nearest thing to an explicit plan and organization of such a business ring in a democracy. There appears to be a sense of anticipation of Schumpeter and Downs on the economic theory of political parties in Veblen's brief comments on parties as business rings. Under constitutional methods, the "ring" of business interests securing the

broadest approval from popular sentiment is put in charge of the government establishment. Parties may gain popular approval on some ground that is extraneous to business policy proper. As examples, Veblen mentioned a wave of national animosity, a particularly popular candidate, or a large grain crop.

But business interests dominate and the political parties competing in elections must recognize that: “. . . the only secure basis of an enduring party tenure of the government machinery is a business policy which falls in with the interests or the prejudices of the effective majority” (Veblen 1915, p. 294).

Veblen evidently anticipated quite clearly the phenomenon of platform convergence that Schumpeter noted much later. “Political parties differ in their detailed aims, but those parties that have more than a transient existence and superficial effect stand for different lines of business policy, agreeing all the while in so far that they all aim to further what each claims to be the best, largest, most enduring business interests of the community” (Veblen 1915, pp. 293–294).

IV

A Second Theory of Governmental Failure

VEBLEN MADE THE CASE very strongly that business men have a firm and effective control over government:

. . . Constitutional government has, in the main, become a department of the business organization and is guided by the advice of business men. The government has, of course, much else to do besides administering the affairs of the business community, but in most of its work, even in what is not ostensibly directed to business ends, it is under the business interests. It seldom happens, if at all, that the government of a civilized nation will persist in a course of action detrimental or not ostensibly subservient to the interests of the more conspicuous body of the community's business men. The degree in which a government fails to adapt its policies to these business exigencies is the measure of its senility (Veblen 1915, p. 287).

But just a few pages later, Veblen described a case of government pursuing policies that harmed the businessmen.

That case involved the emergence of a Leviathan-type government. In the modern world market situation, governments engage in war and armament expenditures as part of an overall strategy to benefit the large business interests of the respective nations. Up to a certain point, such expenditures yield positive pecuniary gains, at least for those firms involved in international markets and production of armaments. But such expenditures and attendant policies have expanded to such a point that they now cut into the aggregate gains of the businessmen. This had already happened in Italy, France, and Germany, and Veblen saw no reason why England and America “should not likewise enter on

a policy of emulative exhaustion, and so sacrifice their aggregate industrial and business interest to the furtherance of the 'great game' " (Veblen 1915, p. 299).

Veblen gave several reasons why the business community failed to call a halt to the excessive war expenditures before the critical point was reached. Those reasons reflected a curious mix of his own unique evolutionary social theory and an anticipation of several elements of modern economic theories of political behavior. The Leviathan government that emerges in Veblen's discussion of excessive war expenditures behaves in a fashion somewhat similar to modern concepts of Leviathan governments, *i.e.*, grows inexorably and evidently cannot be controlled by the ordinary democratic election/legislative processes. But it is not a rational government in that its growth may well destroy the private sector that sustains it. There is "a fair chance of ultimate exhaustion or collapse through the bankruptcy of the State" (Veblen 1915, p. 300).

The origin and nature of this Leviathan State was explained in pure Veblenian terms. It represents a revival of the dynastic State, the product of atavistic habits and barbaric sentiments which have been incompletely eroded by the forces of modern machine technology. The growth in military preparations and armament expenditures revived a barbaric warlike animus on part of the populace and the atavistic habit of arbitrary autocratic rule with unquestioning enthusiastic subservience on part of the subjects. As the dynastic State with its militant code of honor and predatory behavioral tendencies reemerges, the ascendancy of dynastic politics reduces business interests to the status of being simply the fiscal ways and means. Business traffic becomes subservient to "higher ends" (Veblen 1915, p. 300), and may be sacrificed if necessary to achieve those ends.

Modern public choice economists would be much more comfortable with Veblen's other (albeit minor) two reasons why businessmen had lost effective control over government. Modern theories stress the role of individual decisionmakers in government who have their own utility functions to maximize within the constraints imposed by their positions. Increasingly large budgets are frequently a means of satisfying those utility functions. In a somewhat similar vein, Veblen remarked that the excessive growth in military expenditures was due in part to an expanding official class's need for increasing emoluments and a larger field of employment and display (Veblen 1915, p. 299). Implicit in that statement is the premise that these government officials are able to manipulate governmental decisionmaking processes to achieve their own goals.

The impression that Veblen anticipated the concept of governmental officials responding to personal economic motivations is reinforced by an observation in the form of a footnote comment. Armament expenditures were described as having a secondary attraction to businessmen of "a more intimate kind," namely, the opportunity for enterprising business firms to engage in peculiarly lucrative

transactions created by the nature of the contract negotiations. Government officials in charge of such transactions have “less than the usual incentives to bargain closely, or to give close surveillance of the execution of the contracts, having no private gains or losses immediately involved” (Veblen 1915, p. 296).

In this discussion of why businessmen lose control of the government, there is also a perception of the political processes failing to channel the short-term self-interested decisions of individual economic agents (businessmen, in this case) into an overall maximization of collective benefits.

One reason why business men fail to check government expenditures on war and armaments is because business enterprise is an individual matter rather than a collective one. As long as an individual business man can realize profit for his firm in meeting the demands for war, he readily responds. His quest for short-term profits blinds him to the long-term consequences of his actions. As long as the pecuniary inducements offered by the government exceed the inducements offered by alternative lines of employment, the businessmen will individually supply those demands, regardless of the ulterior substantial long-run outcome (Veblen 1915, pp. 300–01).

V

Governmental Failure in Veblen's Later Works

VEBLEN'S GENERAL THEORY that democratic governments function on behalf of business interests at the expense of the vast underlying population was repeated forcibly and expanded upon in his later works. In *The Vested Interests and the Common Man* (1919), Veblen described “democratic sovereignty” as having been converted “into a cloak to cover the nakedness of a government that does business for the kept classes” (1946, p. 125). The common man irrationally thinks that he comes in for a “ratable share” of the “imponderables”, *i.e.*, the illusion of property in the form of national prestige and honor. The government procures and safeguards foreign investments and concessions for the businessmen and the burden of the cost falls on the unprotesting common man. Subsidies and credits are provided to those businessmen who profit from shipping and the cost is willingly borne by the common man. Colonies are procured and administered at public expense for the private gain of certain traders, concessionaires and administrative office-holders, the cost of which is willingly borne by the common man (Veblen 1946, pp. 136–37).

The only difference between the dynastic State and the democratic commonwealth is that in the latter “the common man has to be managed rather than driven—except for minor groups of common men who live on the lower-common levels, and except for recurrent periods of legislative hysteria and judiciary

blind-staggers" (Veblen 1947, p. 127). Such management of the common man by the governmental representatives of the businessmen is not difficult to achieve as "he is helpless within the rules of the game as it is played in the 20th century under the enlightened principles of the 18th century" (Veblen 1946, p. 163). A remark in *Absentee Ownership* vividly describes the pathetic case of the common man:

An illustrious politician has said that "you can fool all the people all the time," but in a case where the people in question are sedulously (sic) fooling themselves all the time the politicians can come near achieving that ideal result (Veblen 1938, p. 34).

In *The Theory of Business Enterprise*, Veblen emphasized governmental aid to business interests primarily in the form of safeguarding the pecuniary rights of property and the tariff. In *The Engineers and the Price System*, tariffs continued to provide the "great standing illustration" of how government assists businessmen, but several other examples were cited of policies that aid business at the expense of the common man. In modern terms, these policies would be analyzed under the heading of "rent-creating" measures, but Veblen described them under the general heading of "sabotage," a conscientious withdrawal of efficiency to enhance the pecuniary values of outputs.

While the private producers practice 'sabotage' on a routine basis, their efforts fail to produce retardation of the industrial processes on a sufficient basis to maximize pecuniary gains. Under the new industrial order: "The needed sabotage can best be administered on a comprehensive plan and by a central authority, since the country's industry is of the nature of a comprehensive interlocking system. . . ." (Veblen 1940, p. 18). In a "civilized nation," the national government has the general care of the nation's business interests in its charge and is in a position to "penalize excessive or unwholesome traffic." Hence, the "nation's lawgivers and administration will have some share in administering that necessary modicum of sabotage" needed to assure maximum pecuniary gains for the businessmen (Veblen 1940, p. 19).

In addition to tariffs, excise and revenue-stamp regulations have the effect of 'sabotage,' although they are not always levied for that purpose. Veblen also cited the prohibition (partially or fully) of alcoholic beverages, and the regulation of trade in tobacco, drugs, poisons, and explosives as having the effect of 'sabotage.' Regulations such as the oleomargarine law and "unnecessarily costly and vexatious routine inspection of industrial (denatured) alcohol" benefit producers of other competing goods (Veblen 1940, pp. 20–21).

Some of the government's 'sabotage' policies were of an anti-Leviathan nature. Veblen observed that government operations could be too efficient for the good of the business enterprise system. Consequently, public use of some public

services needed to be discouraged. Thus, the “singularly vexatious and elaborately imbecile specifications that limit and discourage use of the parcel post” were for the benefit of private express companies and other carriers that had a vested interest in such traffic. Moreover, with the federal take-over of the express companies and railroads during the war, a comprehensive system of vexation and delay in “detail conduct” was implemented to discredit federal control of such traffic and to provoke strong public support for a speedy return of these operations to the private sector (Veblen 1940, pp. 21–22).

In *Absentee Ownership*, Veblen cited several other examples of policies that aided business. The Federal Reserve served the “One Big Union” of investment bankers who had come to control the business enterprise system (Veblen 1938, p. 390). The policy of guaranteed earnings for American railroads was simply a subsidy for the owners. The railroads had ceased to earn returns on investment, and consequently, their highly capitalized values should shrink accordingly. But the guaranteed earnings by the regulatory commission meant that the shrinkage was simply made up by the taxpayers (Veblen 1938, pp. 184–85). In addition, Veblen cited the use of the “Intelligence Service of the Army” to keep dissident workers in line as a benefit provided to employers (Veblen 1938, p. 434).

VI

Some Neglected Insights

WHILE VEBLÉN'S GENERAL THEORY of government serving the pecuniary interests of the business community ran consistently through Veblen's later works, the other concepts of political behavior and governmental failure found in *The Theory of Business Enterprise* either disappeared or were rejected. No further mention is found of political parties as competing “rings” of business interests with platforms that tend to converge, yet remain sufficiently distinct to attract votes. Veblen did mention a “One Big Union of Interests” in *Absentee Ownership*, but this involved a tacit understanding among big business interests and investment bankers, not party platforms. In view of the conspicuously irrational behavior of politicians (and voters) in campaigns, it seems odd that Veblen did not delve more deeply into the nature of party competition.

The suggestion that government officials may pursue their own self-interests within the opportunities provided by their positions evaporated more slowly. There are several hints in *The Engineers and the Price System*, *The Nature of Peace*, and *The Vested Interests and the Common Man* that public policies reflected at least in part personal gains for public officials. Colonies procured and administered at public expense were for the private gain of “administrative

office-holders” as well as private traders (Veblen 1946, p. 137). The material interests that impel nations to declare war have only imaginary net value to the community but “may serve the interest of officeholders” (Veblen 1919, p. 24). One of Veblen’s more explicit comments relating to the economic interests of officeholders is found in *The Nature of Peace*:

The only other class, besides the preferentially favored businessmen, who derive any material benefit from this arrangement is that of the officeholders who take care of this governmental traffic and draw something in the way of salaries and perquisites (Veblen 1919, p. 26).

A particularly interesting suggestion in Veblen’s later works that government officials may have individual utility functions is found in *The Engineers and the Price System*. Not only does the Administration employ policies of “sabotage” for the benefit of businessmen, it does so to promote its own interests. This occurs primarily in the arena of information and censorship of that information for allegedly national security reasons.

. . . The ordinary equipment and agencies for gathering and distributing news and other information have in the past developed a capacity far in excess of what can safely be permitted . . . Even the mail service has proved insufferably efficient, and a selective withdrawal of efficiency has gone into effect . . . (Veblen 1940, pp. 23–24).

These wartime censorship measures and the “selective withdrawal of efficiency” in the postal service was calculated to serve the interest of the Administration: “. . . It has been found best to disallow such use of the mail facilities as does not inure to the benefit of the Administration in the way of good will and vested rights of usufruct” (Veblen 1940, p. 24).

But in *Absentee Ownership*, Veblen’s last book, individuals in governmental positions appear to have no purpose other than to faithfully serve the interests of the businessmen. The type of people administering governmental agencies constituted a “businesslike personnel, imbued with the habitual bias of business principles” who are drawn from the business community (Veblen 1938, p. 404). In a footnote comment, he observed that legislators, executives, and judiciary are similarly imbued with the habitual bias of businesslike principles as a result of their conditioning under the price system (Veblen 1938, p. 404).

In *Absentee Ownership*, the businessmen are firmly and completely in control of government, so much so that:

. . . The constituted authorities of this democratic commonwealth come, in effect, to constitute a Soviet of Businessmen’s Delegates, whose dutiful privilege it is to safeguard and enlarge the special advantages of the country’s absentee owners (Veblen 1938, p. 37).

In a footnote comment, Veblen observed that:

. . . It is the boast of the present, latest and presumably best, Federal Administration in this country that this is altogether a Business Administration; and this is no idle boast. Its legal findings as well as its legislative and administrative measures have run admirably true to the

form so set up. Always, night and day, the peculiar care of the Administration is now and ever shall be the profitable activity of the nation's business concerns, more particularly the larger concerns with a large capitalisation and a substantial rate of earnings (Veblen 1938, p. 37).

Completely missing is the concept of a Leviathan-type government resting on revived barbaric habits and atavistic sentiments and threatening harm to the business interests by excessive military expenditures. What happened to Veblen's "second theory" of governmental failure that was introduced in *The Theory of Business Enterprise*? In *The Nature of Peace*, Veblen flatly contradicted his earlier premise that military expenditures could get out of the control of businessmen.

In these democratic countries public policy is guided primarily by considerations of business expediency, and the administration, as well as the legislative power, is in the hands of businessmen, chosen avowedly on the ground of their businesslike principles and ability. There is no power in such a community that can over-rule the exigencies of business, nor would popular sentiment countenance any exercise of power that would traverse these exigencies, or that would act to restrain trade or discourage the pursuit of gain. An apparent exception to the rule occurs in wartime, when military exigencies may over-rule the current demands of business traffic; but the exception is in great part only apparent, in that the warlike operations are undertaken in whole or in part with a view to the protection or extension of business traffic (Veblen 1938, p. 156).

Why did Veblen reject his earlier thesis that government may become a Leviathan that uses business interests rather than serving those interests? Various comments in *The Nature of Peace* suggest that he viewed the actual wartime activities as substantially eroding those vestiges of archaic habits of subservience and dynastic politics that were revived in the pre-war military build-up. As would be expected in Veblenian social theory, the root factor in that erosion was the influence of modern industrial technology.

One chapter of *The Nature of Peace* was entitled "Elimination of the Unfit," which described the general institutional effect of the war on the mentality of the participants. At one point, Veblen discussed the fate of the British "gentlemen" officers on the modern battlefield.

. . . The war has turned out not to be a gentlemen's war. It has on the contrary been a war of technological exploits, reinforced with all the beastly devices of the heathen. It is a war in which all the specific traits of the well-bred and gently-minded man are a handicap; in which veracity, gallantry, humanity, liberality are conducive to nothing but defeat and humiliation (Veblen 1919, p. 245).

The thrust of this discussion is that the romantic myths underlying dynastic politics, reflected in armies led by "gentlemen" bringing national glory and honor by their gallant exploits on the battlefield, had been blown away by the reality of modern technological warfare. Veblen emphasized that:

Modern warfare and modern industry alike are carried on by technological processes subject to surveillance and direction by mechanical engineers, or perhaps rather experts in engineering science of the mechanistic kind. War is not now a matter of the stout heart and strong arm. Not that these attributes do not have their place and value in modern warfare; but they are no longer the chief or decisive factors in the case. The exploits that count in this warfare are technological exploits; exploits of technological science, industrial appliances, and technological training. As has been remarked before, it is no longer a gentlemen's war . . . (Veblen 1919, pp. 303–04).

The growing importance of technology in war has several ramifications upon the conduct of government policy. While it erodes the status of the “gentlemen” aristocrats as leaders, it increases the roles of technicians and engineers. The result is threatening to the social leadership:

. . . The blameless, and for the purpose imbecile, executive committee of gentlemen-investors has been insensibly losing the confidence and the countenance of the common man . . . (Veblen 1919, pp. 250–251).

The future appeared to be threatened by an awakening of the common man to the true nature of affairs.

This shifting of discretionary control out of the hands of the gentlemen into those of the underbred common run, who know how to do what is necessary to be done in the face of underbred exigencies, may conceivably go far when it has once been started, and it may go forward at an accelerated rate if the pressure of necessity lasts long enough. If time be given for habituation to this manner of directorate in national affairs, so that the common man comes to realize how it is feasible to get along without gentlemen-investors holding the discretion, the outcome may conceivably be very grave (Veblen 1919, pp. 251–52).

The prospect that the war conducted along technological lines might be breeding rationality on part of the common man was sufficient to induce the businessmen to recognize the importance of bringing government under control and ending the war. To allow it to continue would mean progressive loss of confidence in “gentlemen governments” and a growing realization among the underlying population that the entire structure of pecuniary property rights and free income rested on a myth.

There was also a lesson learned about the effect of war finance on the credit system. In *The Theory of Business Enterprise*, Veblen held out the prospect of national bankruptcy as war and armament expenditures rose. But in *The Nature of Peace*, he remarked “The war experience has hitherto gone tentatively to show that funds and financial transactions, of credit, bargain, sale and solvency, may be dispensed with under pressure of necessity; and apparently without seriously hindering that run of mechanical fact, on which interest in the present case necessarily centers . . . (Veblen 1919, p. 253). Veblen went on to observe that: “When . . . the national establishment becomes sufficiently insolvent, it is beginning to appear that its affairs can be taken care of with less difficulty and

with better effect without the use of financial expedients" (Veblen 1919, p. 253). This exposure of the weak link between finance and the real industrial economy lessened the danger to the business enterprise system of a national expenditure policy leading to bankruptcy, even if at the same time it exposed the true nature of financial investment to the economic system.

In *Absentee Ownership*, a somewhat different view of the disappearance of the threat to the business enterprise system from war expenditures can be gleaned. After 1913, there was really little prospect that in the U.S. military expenditures could lead to bankruptcy of the State simply because the Federal Reserve could provide credit to both the government and the investment banks. This enabled the government even during war to be conducted on more business-like terms, and with businessmen in control.

VII

Concluding Statement

VEBLEN'S CONCEPTS of governmental failure would appear to merit the critical attention of modern institutionalists. In particular, his general theory suggests an avenue of study that could yield valuable insights into the governmental policies of the 1980s. Veblen's concept of social welfare provides a normative basis for critiquing the goals and values of the "Reagan Revolution." His concept of voters irrationally endorsing policies that benefit the vested interests provides a more realistic approach to explaining the popular support for Reagan, and the willingness of many voters to believe that the federal budget can be balanced by increasing defense spending while cutting taxes on the higher income groups, or that poverty and inequity can be eliminated by reducing expenditures for domestic social programs.

On a historical basis, Veblen may have failed to realize the power of his theory of a Leviathan government growing beyond the control of the vested interests. In terms of subsequent world developments, the tragic case of Hitler coming to power in Germany is a classic example of such a Leviathan government. Voters in the Weimar Republic allowed the vested interests to exploit their nationalistic fervour and fears, thus allowing Hitler's Nazi party to come to power by constitutional means. The business/industrial leadership assisted the Nazi leader, assuming they could control the dictatorial regime that was implemented. Ultimately, their economic interests were sacrificed along with the rest of Germany as the Hitler Leviathan proved to be uncontrollable.

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Who Will Pay?

HOW DO WE DELIVER LONG-TERM CARE to the elderly as their number increases? How do we finance the rising costs? Should the responsibility be assumed by the public or the private sector?

Alice M. Rivlin and Joshua M. Weiner have examined these questions in *Caring for the Disabled Elderly: Who Will Pay?* (Washington, D.C., The Brookings Institution, 1988, \$29.95 cloth, \$11.95 paper).

Raymond J. Hanley and Denise A. Spence, of the Brookings Economics Studies Program, explore the potential of the private sector and the options of the public sector. Their recommendations for financing long-term care are especially important since this problem increases with each passing year.

C.E.G

Effort and Care

ALL THE GREAT SOURCES of human suffering are in a great degree, many of them entirely, conquerable by human care and effort.

JOHN STUART MILL