

Karl Polanyi – The Great Transformation (1944)

The Lowdown: The intrinsic processes of the 19th century economic system were the mechanisms of its own destruction. To the degree the liberal market expanded in industrial Europe, it created counterpressure among the social groups most vulnerable to its excesses, especially labour. As labour mobilized, it increasingly sought through politics the social protection that the economic order could not provide, but in so doing undermined the market system itself. As these groups gained the franchise, noninterventionist policies became harder to maintain. Liberals rallied around the gold standard as the critical feature of the economic system, and sacrificed everything, including the free market, in a vain attempt to sustain it. Polanyi concludes that the nineteenth century proved unstable the utopian dream of the self-regulating market, and the future economic order cannot make the mistake of institutionally separating politics from the economy.

The Four Features of the 19th Century Economic System:

- 1) The Balance of Power (political, international): Prevented any Great Power wars during the course of the 19th century. “The Hundred Years’ Peace” does not imply the lack of wars on the periphery, or between a Great Power and a small state, but does preclude the large-scale wars that are bad for business. Note that usually war is the mechanism that preserves balance of power, but here peace is the norm. The rise of an acute peace interest among “that cartel of dynasts and feudalists whose patrimonial positions were threatened by the revolutionary wave of patriotism that was sweeping the Continent” worked as a substitute for war as the mechanism of maintaining balance.
- 2) International Gold Standard (economic, international): Allowed the self-regulating market to transcend national borders and work at the international level. The gold standard ensured convertibility of currencies, reducing transaction costs that might otherwise render trade unprofitable. Considered the lynchpin of the entire international order, liberals would sacrifice the other three features of the economic system to save it. In the 1930s, both the US and Great Britain abandon the gold standard, effectively severing all connection to the 19th century order.
- 3) Self-Regulating Market (economic, domestic): The “utopian dream” of the 1800s according to Polanyi, the self-regulating market is economics completely divorced from politics. Though enormously productive and profitable to an industrial elite, the market made the lower classes highly vulnerable to its instabilities. Polanyi sees a flaw in the system in that it treats labour as a commodity, when labour will not allow itself to be treated as such.
- 4) Liberal State (political, domestic): Seen as a creation of the self-regulating market. Provided the laws (or lack thereof) governing the market economy. The liberal state was most consistent with the self-regulating market when government participation was limited to those who most benefited from the market. As the vote expanded to labour and other classes vulnerable to it, the tension between democracy and the market began to rip the system apart.

The End of Utopia:

Throughout the 19th century, as the economic system was running on all cylinders, the early questions concerning the legitimacy of capitalism as social order disappeared. Chief among those concerns was the legitimacy of the institutional separation of politics and economics. When English parliament refused the Chartists participation in 1832, and repealed the Speenhamland Law in 1834, this institutional separation ceased to be an academic issue. A whole new interpretation of the poor appears. The pauper deserved relief for the sake of humanity, but the unemployed, for the sake of industry, did not. But the more labour was squeezed, the more it demanded the vote. As it gained power in government, labour pushed for interventionist policies for the sake of social welfare, but in doing so undermined the market system that required the commoditization of labour to function. As the system deteriorated, governments did whatever they could to maintain the gold standard, eventually eliminating the balance of power (impositions on Germany following WWI), the self-regulating market (state interventionist policies), and the liberal state (rise of fascism) in order to save it. By the 1930s the Americans and British finally abandoned gold to avoid these sacrifices. With the last feature of the Old World economy destroyed, the next international economic system must learn from the mistakes of its predecessor to avoid a repetition of history.

Theoretical Lessons:

The 19th century demonstrated the weakness of the self-regulating market as a ruling social principle. The true criticism of the market is that it is based on self-interest and is therefore an unnatural foundation for a society. The institutional separation of politics and the economy bought a peculiar form of freedom, but did so at the costs of justice and security. The end of the 19th century economic system leads to either fascism or a new conception of liberalism. Fascism, like socialism, merely responds to dissatisfaction with the malfunction of a market system. Socialism simply connotes the subordination of economics to politics, but fascism entails the reform of the market system at the expense of all democratic institutions. A truly self-regulating market will never again be the core of the international order because labour, land, and money have been pulled out of the market.