

ALFRED MARSHALL'S SYSTEM OF ECONOMIC FREEDOM

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## CHAPTER I

### INTRODUCTION

During the first half of the Nineteenth Century, most of the important discussions of technical economic matters in England took place among men of affairs and men of letters. But during the second half of the Century, these discussions increasingly began to fall into academic hands. Cambridge of the English Universities had established its preeminence in the development of economic thinking by the 1880's; and that preeminence was assured by the unique position occupied by Alfred Marshall in the evolution of political economy.

Not long after Marshall returned to Cambridge as Henry Fawcett's successor in 1885, he began an agitation to establish Economics as a separate Tripos. He was largely responsible for the organization of the Royal Economic Society. His work on several Royal Commissions, particularly the Commissions on Gold and Silver and the even more important Commission on Labour, led to a general recognition and appreciation of his work in economics. Above all, the publication of the *Principles of Economics* and its acceptance throughout the English speaking world brought to Marshall such a supremacy in the field that R. F. Harrod could recently say: ". . . economics at Cambridge had for long been dominated, and was for long to continue to be dominated, by the personality of Alfred Marshall."<sup>1</sup> Harrod might justifiably have extended his remark to include economic thinking in all of England at least until the publication of *The General Theory of Employment, Interest and Money*.

Marshall's importance as an economist would certainly be enough to justify a critical consideration of his work. From a personal point of view, I have been particularly taken with Marshall as the subject for analysis because he represented the apogee of economic thinking in the Victorian period in which I have always been interested; and Marshall, like his age as a whole, was to cast his shadow far into our own Century. The

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<sup>1</sup> R. F. Harrod, *The Life of John Maynard Keynes*, (New York: Harcourt, Brace and Co., 1951), p. 142.

hallmark of the Victorian economists was their insistence on treating the moral characteristics of the individual, his tastes and preferences, as a part of the general system of analysis. The claim of the Victorians—that it was possible to deal with the problem of the social and psychological well-being of individuals in terms of their relationship to economic activities—has been carefully ignored by their successors or at best treated as one of the peculiarities of the manners of the time. The abandonment on the part of the post-Marshallian theorists of any systematic attempt to deal with the dimensions, other than in terms of price and quantity, through which an individual may adjust to his economic environment has certainly been one of the important elements in the failure of the post-Marshallian writers to develop an adequate theory of progress or, with the notable exception of Schumpeter, to attempt such a development. There is real poignancy in a remarkable confession of Joan Robinson, certainly one of the most important of the post-Marshallian writers, that some twenty years of her professional career were in a measure wasted: [2]

At this point, it seems to me now that I took the wrong turning. Professor Pigou had long since worked the hard core of Marshall's analysis into a logical system of static theory . . . Instead of abandoning the static analysis and trying to come to terms with Marshall's theory of development, I followed Pigou and worked out the *Economics of Imperfect Competition* on static assumptions.<sup>2</sup>

The primary purpose of this study will be to try “to come to terms with Marshall's theory of development” and the system of analysis Marshall evolved for dealing with economic problems in the context of historical change. In the examination of, the elements constituting that system of analysis, the genesis of Marshall's thinking will be emphasized, though much attention will be given to its logical organization.

The genetic approach in critical analysis is made much easier when the subject has been explicitly and extensively set forth so that the necessity for deducing connections between the subject and the relevant data is minimized. In this regard, Marshall has

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<sup>2</sup> Joan Robinson, *Collected Economic Papers*, (New York: Augustus M. Kelley, Inc., 1951), pp. vii-viii.

proved especially adaptable to a genetic approach, for he was by nature a systematic thinker. That is, he attempted to assign a proper place in his intellectual scheme to all of his beliefs and ideas. He was never content with inconsistency but felt compelled, to search out reconciliations. These reconciliations were quite formidable, for Marshall possessed technical qualifications in history, mathematics, philosophy, and a knowledge of industrial organization and practices second to none of his contemporaries. True, Sidgwick may have been <sup>[3]</sup> a more subtle philosopher, Cunningham the better historian, Edgeworth the more powerful mathematician, and Walter Bagehot may have possessed a more intimate knowledge of trade practices; but none of this group was the equal of Marshall taking all these fields together.

Marshall accepted in large measure the tradition of English rationalism current in his time. This fact, coupled with the systematic character of his thinking and his wide knowledge, resulted in a reflection in his writing of the predominant modes of thought in England in the last half of the Nineteenth Century. And because of the high order of his analytical ability, he expressed those modes of thought with a clarity which greatly simplifies the task of tracing their development.

The statement that Marshall reflected the predominant modes of thought of his time deserves important qualification: Only to the extent that the middle class in England represented in its outlook the most important historical tendencies is this statement correct. For Marshall, even when judged solely in light of his effect on subsequent economic thinking, was, during his day, one of the most important and influential proponents of middle class economic philosophy. The "middle class" is here taken in a conventional sense as referring to those individuals whose political and social interests and incomes are connected with or derived from the ownership or management of the methods of production which began to predominate with the industrial revolution.

Marshall stands at the midpoint of an economic tradition of the middle class which found its first, complete expression in Ricardo and <sup>[4]</sup> perhaps its latest in John Maynard Keynes. The animus for much of the former's work had been provided by a profound

distrust of the landed interests and their political and economic prerogatives. Ricardo felt that the protection of the value of land through the system of corn law quotas and tariffs was endangering the prosperity of England. The only escape, he felt, from the long run pressures of population and the "iron law of wages" lay in the unrestricted exploitation of the potentialities of the industrial revolution. The struggle against the Tory landed interests ended well before the mid-century point with the accession to political power of the middle class and the end of protection. Ricardo's battle had been won. For a while, there was no serious challenge to the economic and political suzerainty of the middle class.

But there was an enemy, nevertheless. That enemy was poverty, insecurity, social disorganization, and demoralization of much of the population which came about as a result of the industrial revolution. The middle class Englishman who was given to introspection on these matters felt a responsibility for the unfortunate people of his period for his prosperity was in some measure the cause of their destitution. These feelings received powerful sanction during the early part of the Nineteenth Century in the social teachings of the Evangelicals. Not that it was thought that the system of economic control should be significantly changed; rather, it was believed that the individual should be assisted in his attempt to adjust to the system as it existed and such changes as were proposed were for the <sup>[5]</sup> purpose of facilitating the process of adjustment. It is to this stage of the development of the tradition that Marshall belongs.

Marshall could see no worthwhile alternative to the system of economic and political control which he called the System of Economic Freedom. But there were, he felt, real dangers inherent in the System's operation. The first danger was the possibility that the machinery of production might come increasingly under the control of individuals who did not properly understand their responsibilities towards their fellow men or, as Marshall would say, were not fully imbued with the high purposes of economic chivalry. With a Victorian's faith in education and the potentialities for good on the part of individuals, he was generally sanguine about the economic and social future of America

and the Western European nations. As long as the institution of the family remained intact and as long as the economic leaders of the community continued to understand the full implications of the requirement that their interests be identified with those of the society as a whole, the possibilities of moral and economic progress would not be endangered. However, Marshall's misgivings about these two conditions occupied much of his writing.

The economic tradition in whose vanguard Ricardo had stood while it won its battle against the landed interests in England was on the defensive by the time of J. M. Keynes. For the dangers which Marshall feared, though hoping for the best, had finally posed a serious threat to the continued preeminence of that tradition. The long run problem of the distribution of income had not approached a full solution as <sup>[6]</sup> Marshall hoped, and there were serious demands for changing existing institutional arrangements by socializing the means of production. Keynes shared with Marshall a distrust of discontinuous social change; indeed, his theoretical system was devised to deal with the problem of distribution of income (in terms of an emphasis upon the quantity of employment) in an advanced technological society where it appeared that the potentialities for new development had been exhausted.

Keynes' implicit defense of this approach was that the gradual and indirect redistribution of income *via* the mechanism of government fiscal policy was preferable to an immediate alteration of existing economic or political institutions. Thus, the cycle of offensive, consolidation, and defensive in the economic traditions of the English middle class as it developed from Ricardo to Marshall and finally to Keynes was complete.

This study then, from another point of view, deals with Marshall as the principal spokesman of the middle class economic tradition during the period in which the great gains which it had made in the first part of the Century were being consolidated. The economic and social structure of middle class society, or the System of Economic Freedom, was the setting of Marshall's theoretical work as an economist as well as his speculations as a moral philosopher or sociologist. A proper perspective on Marshall's

work as an economist requires, therefore, an understanding of his attitude towards the middle class and his beliefs as to the nature of the middle class. [7]

There are a number of different levels of description applicable to the operation of the System of Economic Freedom. First, the System was treated by Marshall on a technical theoretical level in terms of strictly economic categories such as cost, demand, production, distribution and so forth, all these pointed towards the construction of a general theory of the economic process. An analysis of certain of these categories as they pertain directly to the operation of the System will constitute the subject matter of Chapter III of this study. Marshall's beliefs as to the increasing concentration of industry due to the general prevalence of increasing returns in manufacturing will also be developed in that chapter. In addition, it will be shown that serious misunderstanding can arise as a result of interpreting Marshall's theoretical formulations, particularly the long run normal cost doctrine, in the tradition of static equilibrium analysis rather than in a manner consistent with his theory of progress.

Second, Marshall analyzed the operation of the system as a development of the institutions involved and the relationship between those institutions and individuals. These considerations will occupy Chapter IV. In that chapter, it will further be shown that Marshall's conclusions on a technical theoretical level as to the increasing concentration of industry are also justifiable on the basis of a more general institutional treatment, and that the motives underlying individual behavior, both economic and moral, are directly related to the size of income and the manner in which income is earned. Finally, Marshall's conclusions as to the role of the entrepreneur will be [8] emphasized, for Marshall felt that it was only through the mediation of altruistic and highly moral individuals that social progress could continue.

Third, Marshall dealt with the System of Economic Freedom in terms of the nature of the social structure which underlay it. This analysis of the social structure, which will be discussed in the final chapter, will in turn be related to Marshall's conception of individual morality and the relationship between the individual and society.



Throughout this study it will be necessary to recur to Marshall's treatment of progress at the various levels of description of the operation of the System. Progress for Marshall involved first, the evolution of techniques of production; second, the development of moral and psychological predispositions of individuals; and, third, the development of institutions or "custom." The economic process, production, distribution, and consumption is ultimately considered as it effects the aspects of progress.

Before beginning the analysis of Marshall's System of Economic Freedom, Chapter II considers the evolution of two complexes of ideas without which it would be difficult to understand either Marshall's method of procedure or the peculiarly moral flavor of his systematic work. The first of these is found in the attitude of Marshall and his group towards the world around them, with especial emphasis on the process of continual and continuous evolution and change; the second involves the impact of the Evangelical <sup>[9]</sup> way of life upon Victorian moral and social beliefs. After a discussion of some of the problems of criticism in the study of economic doctrines, the relationship of these two complexes of ideas to Marshall's work will be explored. <sup>[10]</sup>