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PART I

1. Economic competition and market organization: the logic of capitalist collective action

Introduction

In this chapter I argue that capitalist relations of production, besides producing conflicts of interest between workers and capitalists, also produce conflicts among capitalists; and that these latter conflicts, which take the form of economic competition, generate a distinct set of collective action problems for competing firms. By analyzing the structure of these problems and the behavior that they generate, we are led to an enhanced understanding of the manner in which capitalist relations of production structure the political behavior of capitalists.

I begin by recalling Marx's argument that capitalist relations of production have a dual character – that they generate antagonism among capitalists at the same time that they generate antagonism between workers and capitalists. I then suggest that the fact of competition among capitalists undermines some common assumptions about the interests of capitalists. Not only do the interests of individual firms often contradict one another, but it is also sometimes the case that the collective interest of the capitalist class contradicts the interests of individual firms.

Next, I argue that economic competition presents capitalist firms with a series of collective action problems. These are exemplified by price competition. Each firm shares a common interest in a relatively high industrywide price, but it is in each firm's interest to "free-ride" on the cooperation of its competitors and to reduce its own price. If each firm behaves rationally and lowers its prices, the outcome will be suboptimal – a lower level of profits than that which could have been achieved if all firms would have cooperated by keeping prices high.

The main body of the chapter is devoted to analyzing these capitalist collective action problems from a game-theoretical perspective, describing various competitive situations as games played among capitalist firms. This enables us to do two things. First, once we have identified the structure of the game, we can predict the strategy that a rational player will select. Second, we can predict the outcome that will be produced by the combination of these strategies. Of particular interest, of

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course, are those competitive situations that generate suboptimal outcomes because, in these cases, we can expect firms to attempt to transform the structure of their interaction and to try to organize their market, perhaps by appealing to outside actors, including the state, to intervene. An important subset of competitive games of this type includes those markets in which firms have different levels of production costs. In these cases, it is likely not only that the achievement of a collectively optimal outcome will elude the voluntary efforts of competing firms, but that an optimal outcome acceptable to all firms in the market does not exist. Here, the mixed-motive collective action problem becomes a zero-sum game of outright conflict.

Capitalist relations of production and the conflicting interests of capitalists

In the analysis of collective action, the principal problem is to determine under what conditions a group of actors will cooperate in pursuit of a common interest. Our first task in analyzing capitalist collective action, then, is to identify the common interests of capitalists. For most Marxists, and many non-Marxists as well, capitalists are a class whose common interests are rooted in capitalist relations of production. These production relations define a shared interest in high profits and in maintaining control of the production process that opposes capitalists to workers. The principal collective action problem faced by capitalists, in this view, is to organize themselves in defense of those interests that oppose them to workers. There can be no doubt that the conflict between capitalists and workers defined by capitalist relations of production is critically important to our understanding of political life, nor that this conflict generates collective action on the part of capitalists. We would be mistaken, however, if we concluded that the worker versus capitalist conflict was the only politically relevant conflict generated by capitalist relations of production, and that the capitalist collective action problem implied by this conflict was the only one, or even the most important one, faced by capitalists. As Marx wrote in *The Poverty of Philosophy*, capitalist relations of production have two aspects. On the one hand, they define the familiar antagonism between worker and capitalist; however, they also determine a fundamental conflict among capitalists. "If all the members of the modern bourgeoisie have the same interest inasmuch as they form a class as against another class, they have opposite, an-

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tagonistic interests inasmuch as they stand face to face with one another."[1]

Few observers would go so far as to deny that capitalists compete, but this competition is rarely taken seriously by political analysts. When the fact of competition is recognized, it is usually treated as a sideshow, on the margins of the main event, the conflict between workers and capitalists. In this view, economic conflicts among short-sighted capitalists complicate the more important struggle, but they are clearly seen as of secondary importance to it. In fact, economic competition represents a very real high-stakes struggle among capitalists whose most fundamental individual interests are in conflict with those of their competitors, and, sometimes, with the collective interests of their class. It is essential to note that these competitive relations are a constituent element of capitalism – any capitalism. The form of competition, the strength of competitive pressures, the capacity of capitalists to control competition – all of these things have varied greatly both across time and across industries within the same time period, just as the worker–capitalist struggle has varied in form and intensity. But in neither case should the vicissitudes of the surface phenomena deceive us into thinking that the defining relationships of the mode of production have disappeared. Whether the object of our analysis is competitive capitalism, monopoly capitalism, late capitalism, or advanced capitalism, capitalist relations of production define a basic antagonism among competing capitalists.

This competitive antagonism has several important implications for political analysis. First, unlike membership in most other groups, the status of being a capitalist is achieved, not ascribed, and, moreover, it is achieved in struggle against other capitalists. The most fundamental interest of any firm is to continue to exist in the market, and, except during periods of the most extreme political crisis, the major threat to this basic interest of each capitalist in economic survival comes not from workers but from other capitalists.

Second, whatever the common interests are that capitalists share in opposition to other groups, their enjoyment by any firm is contingent upon its successful defense of its market position against competitors. The common interests of capitalists are only "common" to surviving capitalists. Thus, competitive struggles are not secondary to struggles between workers and capitalists, but rather they occupy a position of

[1]Karl Marx, *The Poverty of Philosophy* (New York: International Publishers, 1963), p. 123.

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logical primacy with respect to them.[2] Each capitalist must secure his or her position as a capitalist in the market before he or she can act as a capitalist in any other arena.

A third implication of economic competition is that the interests of individual firms may be incompatible with the collective interest of capitalists in the continued survival of capitalism. In Marx's words, "the individual capitalist is in constant rebellion against the general interests of the capitalist class as a whole."[3] The continued existence of the capitalist system is certainly a necessary condition for the achievement of the firm's interest in economic survival; however, it is not sufficient to ensure the firm's survival. While the continuation of capitalist reproduction ensures that there will be some firms, it does not guarantee the survival of any particular firm.[4] Not only is it a fact of life in capitalist economies that firms sometimes go out of business, but it is in the interest of the preservation of the allocative efficiency of the capitalist economy that this occurs. The reproduction of capitalism – the accumulation of capital – requires capital to be shifted away from less efficient firms and sectors to more efficient ones. Insofar as capital accumulation requires such a redistribution of capital, the long-term reproduction of capitalism implies developments which contradict the interest of some individual firms. Marx writes in *The Poverty of Philosophy* that

> From day to day it thus becomes clearer that the production relations in which the bourgeoisie moves have not a simple, uniform character, but a dual character; . . . that these relations produce bourgeois wealth; i.e., the wealth of the bourgeois class, only by continually annihilating the wealth of the individual members of this class and producing an ever-growing proletariat.[5]

Perhaps the most important implication of competitive relations, and one whose consideration occupies most of the present study, is that in dividing capitalists, economic competition presents them with a set of collective action problems distinct from those they face in their opposition to workers, and which sometimes "overdetermine" these latter problems. Capitalist competition creates a paradoxical situation in which

[2]This expression is somewhat misleading in that the struggle between labor and capital within each firm is part of the competitive struggle between firms. However, it is competition among firms that is the motor behind the labor–capital struggle within the firm. In its absence, capitalists would not be forced to increase the rate of exploitation.
[3]Quoted in Jon Elster, *Making Sense of Marx* (Cambridge: Cambridge University Press, 1985), p. 189.
[4]Adam Przeworski, "Toward a Theory of Capitalist Democracy" (Unpublished Paper, University of Chicago, 1980), p. 24.
[5]Marx, *The Poverty of Philosophy*, p. 123.

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the attainment of each firm's individual interest in profits and economic survival is dependent on the cooperation of its competitors.

Economic competition as a collective action problem

In everyday usage, the verb *to compete* implies rivalry and interdependence among the competing units. Capitalist firms compete when they pursue policies that affect each other's sales. Price cutting, advertising, investment, product differentiation, and so forth are all undertaken with the aim of increasing a firm's market share at the expense of other firms in the market. Curiously, this sense of rivalry and interdependence is absent from the economic theory of the competitive market, where firms respond passively to a set of impersonal constraints which they are unable to affect. "A persistent weakness of the concept of competition," writes Paul McNulty,

> has been the tendency of economists to minimize, ignore, or deny its interdependent nature, that is, the extent to which the competition of one economic unit tends to affect the economic position of others, and, thus, the overall market structure. Despite the etymology of the verb (literally "to seek together"), to compete, in economic theory, has generally meant to act independently.[6]

The basic neoclassical economic model of competition is set in the perfectly competitive market, in which each firm's share of output is so small that an increase or decrease in the quantity that it produces will not affect the price of the commodity. In this type of market, each firm faces a horizontal demand curve (price is therefore a given) and the firm "competes" by setting output at the level at which price and marginal costs are equivalent. A reduction of output from this level would generate a loss of revenue greater than the cost savings of reduced production, and an increase in output would cost more than the revenue brought in by increased sales. Graphically (see Figure 1.1), this quantity $(q)_1$ is determined by the intersection of the marginal cost (MC) and demand (DD_1) curves. The average cost curve (AC) gives the cost of each unit as a function of output. When each competing firm's MC and DD_1 curves are aggregated, the industry supply (S) and demand (D) curves are the result (see Figure 1.2). The downward slope of the industry demand curve reflects the fact that while the price level is not

[6]Paul McNulty, "Economic Theory and the Meaning of Competition," *Quarterly Journal of Economics* 82 (November, 1968): 654. As Joe Bain points out, this interdependence encompasses not only firms within the market, but potential entrants as well (see his *Barriers to New Competition*, Cambridge: Harvard University Press, 1965, p. 4).

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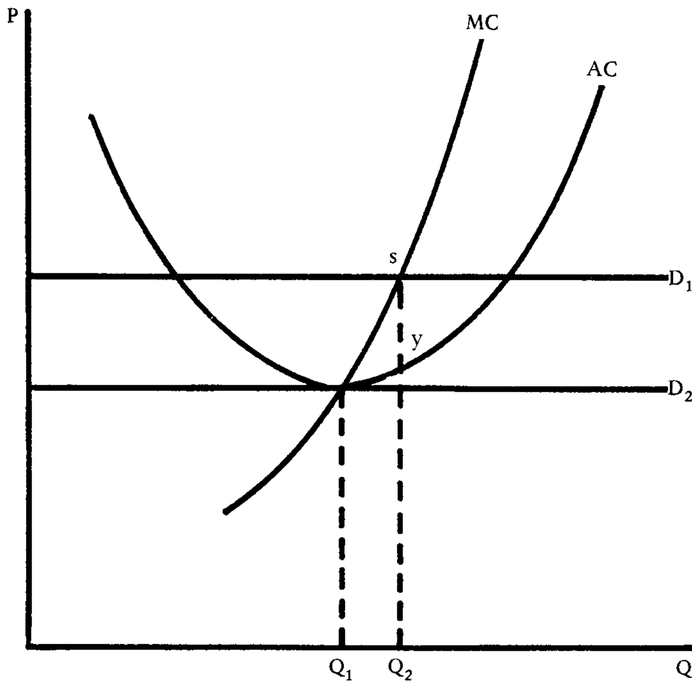

Figure 1.1. The individual firm in the perfectly competitive market. *Source:* Scherer, *Industrial Market Structure*, p. 12.

responsive to the output decisions of the individual firm, it will respond to the industry supply level, which is the aggregate of the output decisions of all of the firms in the industry. If the firm's demand curve cuts the marginal cost curve at a point to the right of the intersection of MC and AC (see D_2 in Figure 1.1), the firm's output will be at q_2. The gap between average costs and marginal costs means that the firm will earn supranormal "economic profits" equivalent to $s-y$ for every unit produced. These high profits will attract new entrants to the industry, causing the industry supply curve to shift to the right (from S_1 to S_2). This increased output will reduce price from p_1 to p_2, lowering the individual firm's demand curve until, at equilibrium, AC, MC, and D intersect (see D_1 in Figure 1.1).

In this model, the individual firm's output level is determined by its marginal cost curve and by the industry demand curve. It chooses an output level, then, independently of its perception of what the other firms in the industry are doing. However, this does not mean that the

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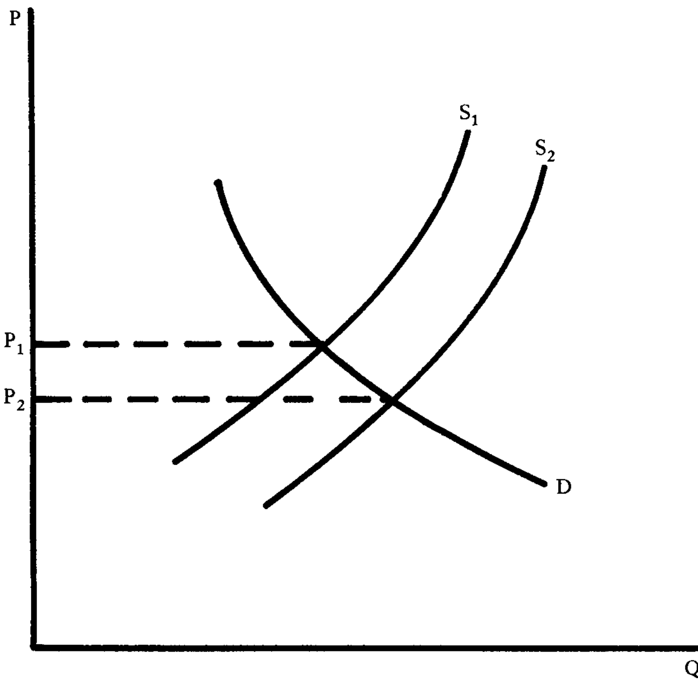

Figure 1.2. The industry in the perfectly competitive market. *Source:* Scherer, *Industrial Market Structure*, p. 12.

behavior of the other firms has no effect on the profit of each individual competitor. The industry price level – a given from the point of view of the individual firm – is in fact determined by the sum of the output decisions of each of the industry's firms. Thus each firm's subjective independence – its inattention to the activities of its competitor – is coupled with an objective interdependence which operates "behind its back." While independently pursuing their own economic survival by selecting the profit-maximizing output level, individual firms are jointly producing the conditions which largely determine both their own economic fate and the fate of their competitors. Capitalist competition, then, has two dimensions. On the one hand it involves the individual, independent pursuit of economic survival through the selection of a profit-maximizing strategy. It is this aspect of competition, which places capitalist firms in conflict with one another, that was the focus of the previous section. On the other hand, competition also involves the joint shaping or "seeking together" by competitors of an economic en-

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vironment in which individual economic survival will be more or less likely. The industry price and output levels are collective goods.[7] Firms contribute to their provision through their price and output policies, and, once they are provided to one firm in an industry, they cannot be withheld from other firms. A firm's success in its struggle against other firms, then, is largely determined by the capacity of the firms as a *group* to "seek together" a benign price and output level.

The fact that the success or failure of each firm depends on the actions of all firms implies that if the firms in the market could communicate with each other and coordinate their activities, they could enhance their collective position. This can be demonstrated graphically with a simple monopolistic pricing model. Figure 1.3 presents the cost, demand, and marginal revenue curves for an industry with the capacity to act in concert as a single monopolistic decision maker. The demand curve (D) is downward sloping, reflecting the fact that the industry as a whole has the capacity to influence price with its output decisions. The negatively sloped demand curve implies a marginal revenue curve (MR) falling to the left of D. This is the critical difference between the industry/monopolist and the individual competitive firm. For the former, facing a horizontal demand curve, marginal revenue (the additional income accruing from the marginal sale) equals price. For the industry as a whole, however, an increase in output can be sold only at a lower price than was previously offered, and, of course, this lower price applies to total, not just marginal, output. Thus the increased revenue from the additional sales is offset in part by the decrease in revenue produced by the across-the-board price reduction that made the increased sales possible. Like the competitive firms, the industry/monopolist maximizes profits by setting marginal revenue equal to marginal cost. However, for the monopolist, this point will not be where the MC and D curves intersect, but where the MC and MR curves intersect. In Figure 1.3, this implies an output of q_1 and a price of W. If price and output were determined competitively, they would be given by the intersection of MC and D: Z and q_2, respectively. The area enclosed by WABZ is the quantity of the "excess" profit available to the firms in the industry if they could act in concert.

In real-world markets, of course, individual firms, however interde-

[7]Mancur Olson defines a collective good as "any good such that, if any person X_i in a group $X_1, \ldots, X_i, \ldots, X_n$ consumes it, it cannot feasibly be withheld from the others in that group "(*The Logic of Collective Action* [Cambridge, MA: Harvard University Press, 1971], p. 14).

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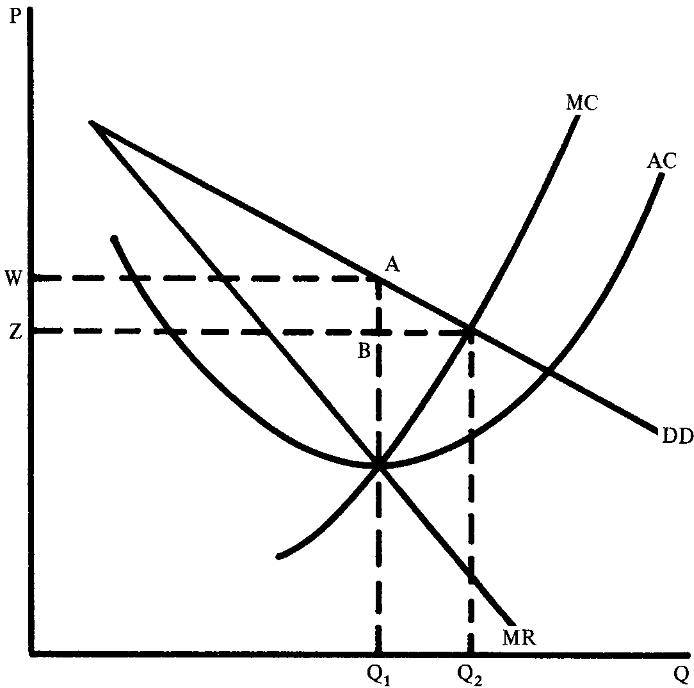

Figure 1.3. The cost and revenue curves of a monopolistic firm. *Source:* Scherer, *Industrial Market Structure*, p. 14.

pendent their competitive situations, retain an independent decision-making capacity. The industry, in other words, consists not of a single, joint decision maker, but of a number of individual decision makers. Dropping the assumption of the unified collective actor completely alters the situation. In this more realistic context, the individual firms face a collective action problem in which the rational pursuit of individual interests interferes with the attainment of a collectively optimal outcome. Return to the market described by Figure 1.3. Clearly, the firms in this situation have a common interest in maintaining the monopolistic price and output level. The relatively high price is a collective good to which each firm contributes with its pricing policy and from which each firm benefits by receiving abnormally high profits. However, as is the case in other collective-good situations, the "enjoyment" of the collective good cannot be denied to any member of the group, whether they contribute to its provision or not, and each member faces a strong in-

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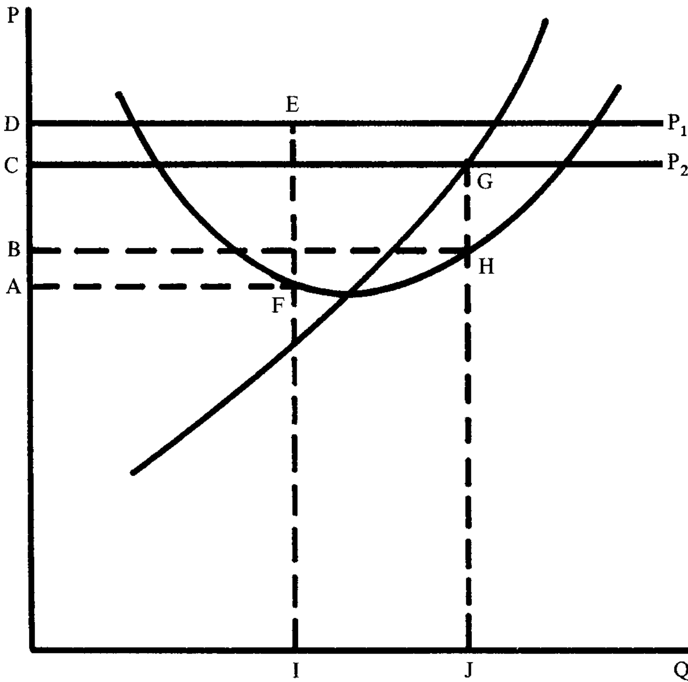

Figure 1.4. Cost curves of an individual firm in a cartelized industry. *Source:* Dewey, *Monopoly*, p. 19.

centive to refrain from contributing, and to free-ride on the contributions of others.[8] In the present case, the temptation is to exploit the high prices charged by competitors and to reduce one's own price and expand one's own output. The result, if all other firms continue their "cooperative" policies, will be higher profits for the price-cutting free-rider. Figure 1.4 shows how each firm can benefit from reducing its price below the cooperative level observed by its competitors. Let us set the cooperative price at D and stipulate that this price implies an output of I from the individual firm. At that price and output level, the firm's profits are equal to the area of DEFA. However, the firm that shades its price below the cooperative level (say, to C) and expands its output to J can increase its profit to the area enclosed by CGHB. The problem is that every firm faces this same temptation, and if each of them yields to it, industry price and output will end up at the competitive level (the intersection of D and MC in Figure 1.3) and each firm's excess profits will be erased.

[8] Ibid.

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