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The authors show that power, in the sense of the ability of one agent to control the behavior of other agents, exists in the capitalist economy, even under conditions of widespread competition and voluntary exchange. This poses a problem for democratic political theory: the capitalist economy is political, but is not a democracy. How do we justify this dichotomy in a society dedicated to realizing substantive democracy where ever unaccountable power is found? Liberal economic theory solves the problem by asserting that economic power is non-existent. "Liberal ...renders the power of capital invisible: democrats cannot assail economic power within liberal theory because they lack the tools for making such power visible." (65-66) This chapter makes the power of capital visible, demonstrating that even a perfectly competitive economy would give rise to pervasive, politically significant, and unequally distributed power.

Introduction: The Failure of Liberal Theory

Two political principles delineate rights in liberal theory. The principle of liberty holds that individuals have inviolate personal rights; the principle of democracy upholds equality and collective popular sovereignty. The public sphere can be defined as those aspects of life where the norms of liberty and democracy both apply, and the private sphere as those where only liberty is applicable. In these terms, any socially consequential exercise of power should be in the public sphere.

Liberal democratic theory supports the application of both principles to the state, but applies only the principle of liberty to the economy; that is, it describes the economy as a private sphere devoid of the exercise of power. This overlooks the fact that power in fact exists in the capitalist economy and is wielded by owners and hierarchically well-planned managers.

The classification of the economy as private rather than public rarely receives an explicit defense; an argument can constructed from two central propositions of neoclasical economics. The first may be called the "labor commodity" proposition: the purchase of labor in an employment relationship has the same character as the purchase of a commodity; there is no exercise of power by buyer or seller in either case. Second is the "asset neutrality" proposition: ownership of productive assets does not convey power, since the competitive pressure of the market dictates economic outcomes. If true, these propositions would support the idea that economic life is private. Yet both propositions are false.

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Understanding Employment

Capitalism is always a system of employment as well as exchange. The asymmetry of the employment relationship has been recognized at least since Thomas Hobbes, (at a time when the terms servant and employee were synonymous) who said, “To have servants is to have power.” The existence of a structure of command within the firm is central to the neoclassical analysis of the firm by Ronald Coase; for Coase the existence of firms proves that it is inefficient to conduct all economic transactions through contractual excange on markets.

Why does it matter that capital hires labor, rather than vice versa? Neoclassical theory has ignored the problem of contract enforcement, which Marx termed the problem of extracting labor (actual productive effort) from labor power (the capacity to work). Employment contracts almost never specify the exact services to be performed; workers are hired to be available for work for a specified time and to submit to the rules and regulations of the workplace during that time. Services delivered by the worker cannot be separated from the person of the worker; and work is almost always a social process involving direct relationships among workers.

These characteristics facilitate worker resistance and thus reader contract enforcement problematic for the employer. There is a tradoff for employers between paying higher wages and subjecting workers to more intense (and costly) surveillance; both are means of eliciting greater effort. Such incentive costs would be lower in a worker-controlled enterprise where identification with the goals of the firm would be greater and the desire to resist work would be weaker.

Power, Production, and Competition

The labor commodity proposition justifies undemocratic, hierarchical organization of enterprises; it claims that racial, sexual, and other forms of discrimination will be eliminated by the market; and it interprets unemployment as voluntary. All of these notions are invalid, and at variance with empirical evidence.

Hierarchical organization is said to be both efficient an unimportant because production is simply a matter of making the optimal choices dictated by the market and the available technologies. Thus the cost-minimizing price and quantity of labor services to be hired by a firm are determined by the market. However, this implies that owners of capital should have little interest in controlling production, since they perform only an externally dictated, technical management function. In practice, this conclusion is obviously false.

The same competitive pressure toward cost minimization should impel the employer to seek the lowest price for an hour of equivalent labor, hiring women or minorities whenever they are paid less than white men. As neoclassical economists have often noted, the market should therefore eliminate wage discrimination; prejudiced employers who persist in preferring higher-wage workers should be eliminated by competition. Again, this is at variance with the facts.

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Likewise, if labor is a commodity, unsold units must have been voluntary withheld from the market. Yet in reality there is a recurrent tendency toward significant unemployment, even in the absence of wage restraints.

The alternative model of labor exchange as a social process involving the exercise of power easily fits all these facts. Hierarchy is of course important to employers seeking to control the labor process. Racial, sexual and other divisions are functional for capitalists because they weaken workers' unity and bargaining strength, and thus decrease the chance of effective resistance to workplace incentives for greater effort. Involuntary unemployment raises the cost of job loss to workers, making the employer's ultimate threat of dismissal a more ominous sanction.

An anomaly in the alternative model is that it suggests that democratic worker-owned firms should be more efficient than capitalist firms, and should therefore outcompete traditional enterprises. The actual scarcity of worker-controlled firms reflects the second dimension of capitalist power, the command over investment.

The Power of the Purse

As Joseph Schumpeter argued long ago, the evolution of new technologies and new forms of organization should, in neoclassical theory, be subject to the same rules: firms that are best able to meet existing market demands will obtain credit, expand their operations, and flourish. In a competitive economy, unsuccessful technologies and organizations, as well as banks that back the unsuccessful, will be squeezed out. Notice that neither financiers nor entrepreneurs exercises real power in this model. If worker-controlled enterprises are efficient, they should thrive.

However, survival in competitive markets is based on profits, not efficiency. Worker-controlled firms may be more efficient in maximizing net output per labor hour, but still produce lower profits. And because they generally start with less capital of their own, worker-controlled firms must borrow more and pay more interest. Financial institutions generally demand either control or collateral in return for funds; a worker-controlled enterprise is ill-equipped to meet these demands.

That is, credit markets routinely violate the asset neutrality proposition. Dealing with their own problems of contract enforcement, i.e. ensuring the repayment of loans, financial institutions act in a decidedly non-neutral manner. They prefer to lend to, and offer the best terms to, those who appear to be the best risks (those who are most able to offer collateral, and most certain to repay). This reinforces existing inequalities and inhibits the entry of new start-up firms into established markets.

Free to Move

Despite the existence of enormous inequalities of power in economic life, liberal theory suggests that economic power can be held accountable to the democratic state. This notion can be faulted on the empirical grounds that the wealthy exercise disproportionate influence through campaign

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contributions, political advertising, lobbying, etc. There is also a deeper problem: capital exerts a kind of veto power over public policy, deriving from the effectiveness of a "capital strike."

By threatening to withdraw investment and move elsewhere, capital can frequently win concessions from the government; a capital strike would impose much greater costs on the incumbent government and the population than it would on the owners of capital. Labor, in contrast, is much less mobile, and is generally constrained to work for some employer in its immediate vicinity. A sovereign state could conceivably change the rules, responding to a capital strike by limiting capital outflow and undertaking public investment. But there are immense practical obstacles to this kind of democratic revolution.

In conclusion,

> Liberal political philosophy is thus curiously at odds with liberal economic theory. The former heralds the individual as an agent empowered to transform his or her world; the latter favors an economic system in which agency is so compromised as to be little more than a false promise for all but the few... By rendering invisible the power of capital, liberal economic theory has contributed more to the legitimation of powerlessness than to making good its claim of universal agency. (90)

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