

Marxian and Non-Marxian Foundations of Rudolf Hilferding's *Finance Capital**

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Abstract:

Finance Capital, written in 1910 by Rudolf Hilferding, is normally understood to be a Marxian work about financial systems, and banks in particular. Because Hilferding was a close friend of his mentor, Karl Kautsky, it is seen as a contribution to the Revisionist Debate within the German Social Democratic Party at the beginning of the 20th century. But this view does not do justice to Hilferding's approach to and objectives for *Finance Capital*. Hilferding took up many ideas from Marxian and Non-Marxian authors like Parvus, Otto Bauer, John A. Hobson, Ferdinand Tönnies, and authors of the emerging corporate finance literature. It is this broad influence that differentiates Hilferding's work from other socialist writings at that time.

JEL Classifications: B 14, B 19, B 31.

I The Theory of *Finance Capital*

In 1910, Rudolf Hilferding published his major work, *Finance Capital*. With this text, Hilferding succeeded in creating an inspiring book that initiated much debate about the power of banks. Hilferding sought to analyze capitalism's development during his time and to integrate his findings into Marxist theory.

Finance Capital presents a cohesive theory in which the topics covered are built up one upon another. He begins by describing the trend of an increased importance being put on the financial sphere, especially banks,

as shown in his money, credit, and bank theories. The second tendency is the increased concentration taking place in the economy, for which Hilferding's cartel theory offers an explanation. He completes his theoretical foundation by bringing together these movements in his theory of "finance capital"; he then applies the results to the business cycle, imperialism, and contemporary political questions.

The text is framed by Hilferding's idea of society's transformation from capitalist anarchy to socialism with an organized economy. Hilferding's idea of *Finance Capital* is based

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on a stage model in which capitalism first supersedes the previous economic order. This early competitive capitalism is analyzed and explained by Marx. But before the socialism phase can begin, capitalism must experience a second phase in which it modifies itself.

II The Creation of *Finance Capital*

Rudolf Hilferding was born on August 11, 1877, in Vienna. In 1893 he joined the "Sozialistischer Studentenbund" (Socialist Student Organization), where he became acquainted with Karl Renner, Max Adler and Otto Bauer. Here Hilferding was exposed to the theories of Karl Marx and Immanuel Kant. In 1899 he was enrolled at the University of Vienna to study medicine. This gave him the opportunity to learn about Carl Menger's new teachings on marginal utility, to learn from Eugen von Philippovich about the Deutsche Historische Schule (German Historical School), and to study Marx's doctrines of labor value (Kurata 1978, 26).

In the winter semester of 1894/95, Hilferding attended Professor Isidor Singer's "sozialstatistische Übung" (social statistics course) and, the following summer semester, the economics course led by Professor Philippovich. He also attended lectures by Carl Grünberg and Friedrich von Wieser, albeit without being officially enrolled (Kurata 1978, 27ff).

In 1903 Hilferding wrote his first article about protective duties and cartels using the example of the sugar industry. He criticized the positive attitude of the revisionist position toward colonialist expansion (Hilferding 1903).

In 1896, Böhm-Bawerk published his ar-

ticle *Karl Marx and the Close of His System*, in which he criticized the theories of Marx and pointed out the transformation problem, since the solution proposed in the third volume of *Capital* (1894) did not provide a sufficient explanation. No later than 1902, Hilferding wrote his anti-critique, *Böhm-Bawerk's Marx Criticism*, and sent it to Karl Kautsky on April 23, 1902, asking for it to be published; however the request was denied. Kautsky said this was due to the essay's length. Nevertheless, Kautsky encouraged Hilferding to continue his Marxist studies (IISG, Karl Kautsky Papers, K D XII 580).

From this time on, a long and close relationship developed between Hilferding and his mentor, Kautsky. Kautsky encouraged him to write regularly for *Die Neue Zeit* (The New Times), of which he was the publisher. In 1903, Hilferding wrote his first articles for this journal on the subject of Marx's theory of value and—in the same year—on the change in function of the protective duty. This was a contribution to the current discussions between revisionists and orthodox members of the German Social Democratic Party (SPD).

The rejection of his essay in *Die Neue Zeit* encouraged Hilferding to create the *Marx-Studien* (*Marx Studies*) series, together with Max Adler, in 1904. These were designed to provide space for medium-length essays with the goal of developing Marxism. Hilferding's article *Böhm-Bawerk's Marx Criticism* was the first to appear in *Marx-Studien*.

Böhm-Bawerk's private seminar in the summer semester of 1905 attracted many prominent participants, including Hilferding, whose names are still remembered today:

Joseph Schumpeter, Otto Bauer, Emil Lederer, Ludwig von Mises, Felix Somary, Karl Pribram, and Otto Neurath. The seminar allowed for an open and intensive exchange of views on economics at that time, Hilferding being one of those representing the Marxist view (Haberler 1950).

In October or November 1906, Hilferding started as one of the two permanent teachers at the newly founded party school of the SPD in Berlin. Hilferding was head of the “Wirtschaftsgeschichte und Nationalökonomie” (economic history and national economics) section, where, apart from studying Marx’s *Capital*, he focused on teaching economic socialism. Even though the Prussian police tried to expel Hilferding from Berlin because of his teaching activities, Hilferding did not go back to Vienna. Instead he continued to work for *Die Neue Zeit* and, in addition, worked as an editor for the foreign policy section of *Vorwärts*, the party newspaper of the SPD. Hilferding rose rapidly within the office and was later promoted to chief editor (Smaldone 1998, 39f).

After 1907, Hilferding published various articles in *Die Neue Zeit* about foreign affairs. In them, he denied the existence of imperialism in Germany in 1907, but in 1909 he realized that there was an increasing danger of war due to imperialism (Stephan 1982, 25f). The arguments he employed could later be found in *Finance Capital*.

Finance Capital was published in 1910. Hilferding had worked on it for a considerable time—the initial work can be dated back to 1902. In a letter to Kautsky in 1902, Hilferding wrote about what he hoped to achieve with *Finance Capital*:

We only have to point to the evidence for the historical necessity of capitalism, to envisage the final goal automatically emerging unaided from the rapid development of late capitalism, and to show that the deliberate waging of class warfare would be a disruptive factor. (quoted in Kurata 1981, 68f—translated from German original)

In 1902, Hilferding used the term “state capitalism” instead of “finance capital” to describe the overall development he diagnosed.

By 1905, Hilferding had at last finished his preparations and started work on *Finance Capital*, having already decided on the name. Thus, he wrote to Kautsky on May 27, 1905:

I am finally going to make a start on my *Finance Capital*, although as yet all I have is the title. (IISG, Karl Kautsky Papers, K D XII 590—translated from German original)

Then, on December 18, 1905:

I also have my *Finance Capital*, which is growing at a slow enough pace, far more slowly than it ought. (IISG, Karl Kautsky Papers, K D XII 598—translated from German original)

Afterwards, on March 10, 1906, he wrote:

In essence I have now completed Chapter I, on money, and will now move on to Chapter II, the role of money in the cyclical process of capital; from this I must then develop the rise and necessity of credit. The tedious thing is that much of

the chapter has to be devoted to restating the contents of the second and third volumes of *Das Kapital* and such repetitive work I find wearisome and uninteresting. (quoted in Kurata 2009, 12—translated from German original)

During his time at the party school and as an editor in Berlin, Hilferding's access to literature—combined with what he learned from his editorial work—allowed him to continue his studies. In the foreword to *Finance Capital*, Hilferding wrote that its main features had already been finished by 1906 (Hilferding 1910, 24). This is evident from the sources he used, since all sources published after 1906 and used in *Finance Capital* are used only for additional or illustrative purposes. Therefore, the main period of time in which *Finance Capital* was written has to be from 1905 to 1906.

III *Finance Capital* as an Attack on Revisionism

In 1891, after the abolition of the anti-socialist law, the newly founded SPD published its new program; it was based on the ideas of Karl Kautsky—his interpretation of Marxism was used as a guideline by the SPD. It was argued that socialism was naturally necessary and inevitable. The party was therefore revolutionary, but did not enforce revolution.

From 1896 onward, Eduard Bernstein published various articles in *Die Neue Zeit* in which he criticized the Marxist foundations of the party. With the encouragement of his friend Kautsky, he summarized these in his book *Die Voraussetzungen des Sozialismus und die Aufgaben der Sozialdemokratie* (The Preconditions of Socialism and the Tasks of

Social Democracy), which was published in 1899 (English translation: *Evolutionary Socialism: A Criticism and Affirmation*, 1911).

Finance Capital is a contribution to the dispute over revisionism, putting Kautsky's side of the argument against his opponents within the party. Accordingly, Kautsky's argumentation in the Revisionist Debate provides the "guidelines" for Hilferding's *Finance Capital*: The cartels are not allowed to prevent crises; the joint stock companies as well as banks are institutions to collect small sums of capital; finance tycoons rule everything; protective duties lead to cheap exports; and the proletariat carry out political revolution (Kautsky 1899). In *Finance Capital*, Hilferding followed these statements precisely.

According to Kurata, Hilferding was especially keen to use *Finance Capital* to refute the revisionism of Bernstein, something which he had already started to do with his critique of Böhm-Bawerk, from whose marginal utility theory Bernstein borrowed some ideas. Kurata noted that *Finance Capital* followed the structure of Bernstein's *Die Voraussetzungen des Sozialismus und die Aufgaben der Sozialdemokratie*. Thus sections II–V of *Finance Capital* are directly comparable to Bernstein's subchapters "2b The Distribution of Wealth in the Modern Community" (especially the meaning of joint stock companies), "2c The Classes of Establishments in the Production and Distribution of Wealth" (especially the question of concentration in the economy and the meaning of the middle class), "2d Crises and Possibilities of Adjustment in Modern Economy," and "3d The Most Pressing Problems of Social Democracy" (especially colonial poli-

tics) (Kurata 1981, 89f).

Kurata's thesis has validity but does not tell the whole story. Of course, the Revisionist Debate is reflected in *Finance Capital* and Hilferding takes an unequivocal stand, but the comparison of thematically similar chapters has the effect of underestimating the significance and the concerns of Hilferding's *Finance Capital*. It is more important to emphasize how much Kautsky's statements in his anti-critique of Bernstein limit the scope of the argument of *Finance Capital*, which engaged with many other Marxian and non-Marxian influences beyond the revisionism issue.

IV Other Socialist Authors

In 1896, Theodor Kapelusz published a series of articles in *Die Neue Zeit* headed "Industrie und Finanz" (Industry and Finance), which cover almost all the aspects that Hilferding would later discuss in *Finance Capital*. The articles are organized in a cursory and primarily political manner, but they can be assumed to have had an influence on Hilferding. In a letter of July 1910, Hilferding states that Kapelusz wanted to receive an issue of *Finance Capital*. He explains that he knows Kapelusz from his visit to the "Freie Vereinigung sozialistischer Studenten" (Bundesarchiv SAPMO—SgY 1 / MS 70 / 8).

Furthermore, influences can not only be seen in the use of the term "finance capital," but also in the discussion of protective duties and capital exports, the importance of monopolies, amalgamation with the state and the importance of high finance. Kapelusz concludes:

Increasingly, the entire economic life is concentrated in the hands of the state; the state is more and more becoming the final court of appeal in the anarchy of the capitalist global market. The state and finance are accelerating and facilitating the transition from the capitalist mode of production to the socialist mode. (Kapelusz 1896, 468—translated from German original)

The emergence of Austromarxism, in which Hilferding played an important part—coinciding with the publication of *Marx-Studien* by Max Adler and Hilferding and the founding of the periodical *Der Kampf* in October 1907 by Otto Bauer, Adolf Braun and Karl Renner—while he was writing his *Finance Capital*, can be seen in this book, and cross-links with other Austromarxist writers can also be found. This is clearest in the case of Otto Bauer. His 1907 study *Die Nationalitätenfrage und die Sozialdemokratie* (The Nationality Question and Social Democracy), which was published by Hilferding as the second volume of the *Marx-Studien*, is quoted on a number of occasions by Hilferding in *Finance Capital* (Hilferding 1910, 311, 335, 344). At the same time he refers to lengthy sections of the book and to Bauer's concept of „Kapitalshörigkeit“ ("enslavement to capital"), which is a fundamental idea in his thinking (Bauer 1907, 216, 292, 316f). Hilferding describes the advantages of large markets, which enable greater specialization and the achievement of returns to scale, referring to Bauer and recommending him for further reading on this topic (Hilferding 1910, 311 refers to Bauer 1907, 148ff). The same applies to the subject of colonial policy, on which Hilferding refers his readers

to one of Bauer's articles in *Die Neue Zeit* if they wish to learn more (Hilferding 1910, 320 refers to Bauer 1908).

This demonstrates that Hilferding regards *Finance Capital* as his contribution to a total view of Austromarxism. As he sees it, Bauer is looking at one aspect of a consistent total theory that he himself is taking in a different direction. For his part, Bauer has been using the term "finance capital" since 1907 (Bauer 1907, 392),¹⁾ a term which he owes to Hilferding, who informed him of his project, including the title, before 1910 (Kurata 1981, 75).

The influence on Hilferding of Bauer's crisis theory, published in *Die Neue Zeit* in 1904, is also evident. In this article Bauer proceeds in a similar fashion to Hilferding in his later analysis in *Finance Capital*: Taking the separation of production and consumption in capitalism as his starting point (Bauer 1904, 134f), he then, building on the second volume of *Das Kapital*, moves on to a detailed cyclical analysis (Bauer 1904, 136ff) and focuses on disproportionality (Bauer 1904, 165). From Bauer Hilferding also adopts the idea that the falling rate of profits, as a consequence of increasing organic composition, is responsible for the sudden transition from prosperity to crisis (Bauer 1904, 166f). At first, Bauer draws attention to the credit system, but he does not enlarge on it (Bauer 1904, 136, 168f). Hilferding saw an opening here to flesh out Bauer's outline with his theory of credit in *Finance Capital*.

Already before 1910, Hilferding was in personal contact with Alexander Helphand (IISG, Rudolf Hilferding Papers), who published under the pseudonym Parvus.

Furthermore, Hilferding quoted from

Parvus's *Die Handelskrise und die Gewerkschaften* (The Trade Crisis and the Labor Unions) of 1901 and *Die Kolonialpolitik und der Zusammenbruch* (Colonial Policy and the Collapse) of 1907. Hilferding also reviewed the latter work in *Die Neue Zeit*. In his review, Hilferding praises the combination of imperialism, protective duties, and the cartels (Hilferding 1907a).

These two writings by Parvus complement each other very well. While the first writing of 1901 exhibits a theoretical derivation and focuses on the relationship with the labor unions, the second is much more empirically organized and focuses on colonial policy. Hilferding quotes from both of them. He used the second publication to comment on the situation in southern Africa, and used the first in relation to Parvus's principal theoretical concern: capital's "*Sturm und Drang*" (storm and stress) phase. This idea is picked up by Hilferding in *Finance Capital* (Hilferding 1910, 318, 320).

All developments in capitalism lead Parvus back to the business cycle. Here, he assumes an overproduction crisis—a disproportion between production and consumption—which does not cause a breakdown of capitalism, but prevents stable production.

The smaller and medium-sized banks fold—and the big banking institutions seize control at their expense. The existing capitalist giants expand at the expense of the collapsed joint stock companies. . . . In short, the trade crisis leads to a massive concentration of capital. (Parvus 1901, 44f—translated from German original)

The concentration of money capital in the

banks leads to concentration of the banks. Industrial concentration resulted from technical development and capitalist competition, but it was significantly boosted by the concentration of money capital—in the banks and in the possession of individuals. (Parvus 1907, 105—translated from German original)

The surpluses have to be invested. This leads to the export of capital:

There are times when the development in all areas of the capitalist economy . . . has reached the stage where a significant expansion of the global market inevitably takes place, and the entire global production is raised to a new and much more comprehensive level. This is the point at which capital enters a period of *Sturm und Drang*. This does not put an end to the periodic alternation of boom and crisis. (Parvus 1901, 26—translated from German original)

Since 1895, according to Parvus, such a phase of “storm and stress” has begun again: imperialism.

With the policy of protective duties, the markets are restricted. The states therefore try to expand in the open colonial areas and integrate them into the protective duties system. Moreover, the state supports the economy with export subsidies.

Parvus also analyses the situation of the banks: The manufacturers and merchants bring their money to the banks or invest it in the stock market, thereby reducing their cash holdings to a minimum. This leads to a competitive relationship between the banks and

the joint stock companies:

The banks, where presently so much of the entire credit is concentrated, have no choice but to raise the interest rate and the discount rate. They have to pay their creditors more, as otherwise the money men would prefer to invest their capital directly in industrial enterprises instead of depositing it in the bank. . . . The joint stock company, although itself fed by the banks, is at the same time a competitor of the bank when it turns directly to the possessors of money and promises them the entire profit from the production. (Parvus 1901, 20—translated from German original)

Both competitions for money capital and reduction of the money capital reserves in industry are dealt with in Hilferding's book.

For Parvus, there is no longer any separation between the banks and industry; instead there is a combined class of capitalists:

The barrier between pure money capital and industrial capital has come down: the banks are in possession of the shares and the liabilities of the industrial enterprises, which themselves own shares in the banks and are represented on their supervisory boards. The whole thing is dominated by the industrial cartels and the bank consortia. The trio is completed by the capitalist state. (Parvus 1907, 105—translated from German original)

Parvus goes further and, using the term „Schwindelgründung“ (fraud foundation), offers a practical explanation of exactly how the process of a higher valuation of the stock

for the appropriation of the promoters' profit—as later described by Hilferding—works:

Even before the factory buildings are finished, before even the smallest quantity of goods have been produced, on the basis of pure speculation it will fix the future profitability of the enterprise in advance and force up the price accordingly . . . it [the joint stock company] must extract this kind of profitability in order to cover the high share price. . . . In this way the stock market drives the new enterprise beyond its original base. (Parvus 1901, 22f—translated from German original)

V John A. Hobson

Hilferding is often associated with John A. Hobson. It is said that Hilferding copied part of the contents of Hobson's *Imperialism*, which was published in 1902. This was never proved but is usually said to be true of a number of socialist theories of imperialism—e.g. by Lenin in 1917 with *Imperialism, the highest stage of capitalism*, who admitted owing some aspects to Hobson.

Did Hilferding take credit for Hobson's studies without admitting it? There is not one quotation or single source that appears in both writings. No issue of Hobson's *Imperialism* can be found in Hilferding's library (Hilferding 1957). The first German translation was only available in 1968. Also, there are differences concerning the content. In Hobson's writing, it is not *Finance Capital* that creates imperialism. Beside economic reasons—especially income distribution—political ambition, excessive patriotism, and a certain amount of philanthropy are also significant.

Nevertheless, Hobson is a major influence on Hilferding. Otto Jeidels, who is an important witness for Hilferding's description of the relation between industry and finance, begins his book *Das Verhältnis der deutschen Grossbanken zur Industrie* (The Relation of the German Big Banks to Industry) in 1905 with a quotation from Hobson's book *The Evolution of Modern Capitalism*, in which he calls for the industrial movement to be regarded from a financial point of view. Jeidels comments:

The tendency toward concentration as a characteristic of modern industrial development is a fact that is now beyond dispute. (Jeidels 1905, 1—translated from German original)

If Hilferding did not know of Hobson's writing by then, this would have prompted him to read Hobson. In fact, an edition of *The Evolution of Modern Capitalism* from 1894 can be found in Hilferding's library. Since more editions were published up until 1910, it is very likely that Hilferding knew of Hobson's writing before 1910. Furthermore, Eduard Bernstein reviewed the edition of 1894 in *Die Neue Zeit* that year (Bernstein 1894). It is most probable that Hilferding was already a reader of *Die Neue Zeit* by that time. In his review, Bernstein introduces Hobson as a socialist.

Hobson defines his concerns as follows:

Since every industrial act in a modern community has its monetary counterpart, and its importance is commonly estimated in terms of money, it will be evident that the growth of capitalism might be studied

with great advantage in its monetary aspect. Corresponding to the changes in productive methods under mechanical machinery we should find the rapid growth of a complex monetary system reflecting in its international and national character, in its elaborate structure of credit, the leading characteristics which we find in modern productive and distributive industry. The whole industrial movement might be regarded from the financial or monetary point of view. But though such a study would be capable of throwing a flood of light upon the movements of concrete industrial factors at many points, the intellectual difficulties involved in simultaneously following the double study, in constantly passing from the more concrete to the more abstract contemplation of industrial phenomena, would tax the mental agility of students too severely, and would greatly diminish the chance of a substantially accurate understanding of either aspect of modern industry. We shall therefore in this study confine our attention to the concrete aspect of capitalism, merely indicating by passing references some of the direct effects upon industrial methods, especially in the expansion and complexity of markets, of the elaborate monetary system of modern exchange. (Hobson 1894, 7)

The following is what Kautsky says about Hilferding's *Finance Capital*:

Of course, the circulation process and the production process are in a constant reciprocal relationship, and the development described above is not produced by the

circulation process alone. The effects of the production process and improved techniques have undoubtedly had a powerful effect, but it would be doing Hilferding an injustice to accuse him of overlooking these factors. It was simply not part of the plan of this work to deal with them in depth. (Kautsky 1911, 767—translated from German original)

Hobson requested others to expand his research on the financial side, while Kautsky asserted that Hilferding wanted to investigate the financial side only. Hilferding therefore organized his *Finance Capital* to be complementary to Hobson's text.

Hilferding's deliberate dependence on Hobson's text is shown in the choice of the subtitle. While Hobson talks about "A Study of Machine Production," Hilferding calls his work "A Study of the Latest Phase of Capitalist Development."

On April 3, 1905, Hilferding wrote to Kautsky:

The adoption of technical and economic institutions in their most complete and finished state is very important for the various forms of economic and political development in different countries. Thus Germany's late [start?] in its capitalist development explains why the development and organization of its banking system is different from that of England. (IISG, Karl Kautsky Papers, K D XII 589—translated from German original)

The topic of Hobson's work is the consequences of technical changes, whereas Hilferding focuses on the financial side of

the capitalist development based on consequences of technical changes.

Hobson's point of view is echoed in Hilferding's article on imperialism for *Die Neue Zeit* in 1907:

Change . . . only comes about with the rapid development of industrial capitalism following the introduction of modern machinery. . . . Industrial capital increasingly dominates commercial capital and interest-bearing capital, which now assumes the form of bank capital. Both forms are coming more and more under the sway of industrial capital. . . . Profits from trade with [the colonies] have now been surpassed by industrial profit from the exploitation of native wage labour. (Hilferding 1907b, 31—translated from German original)

Also, much of the content is very similar. Thus, Hobson says about his methodical understanding:

Science is ever becoming more and more historical in the sense that it becomes more studiously anxious to show that the laws or principles with whose exposition it is concerned not merely are rightly derived from observation of phenomena but cover the whole range of these phenomena in the explanation they afford. (Hobson 1894, 1)

This corresponds with Hilferding's understanding of the national economy as historical science (Hilferding 1904b, 53).

Some of Hilferding's statements can also be complemented and clarified by Hobson. Thus, Hilferding talks about the promoters' profits and says that stocks have the same

characteristics as monetary capital, and therefore compete with the price of free money capital, which is the interest.

Hilferding calls the reduction of the dividend at the level of the interest rate—which is a precondition for his explanation of promoters' profit—a “historical development,” which works alongside the development of stocks and the stock exchange (Hilferding 1910, 109). Therefore, the starting point is the increase of potentially invested financial assets and the increase of free marketability. While Hilferding does not elaborate any further on this historical process, the initial thoughts underlying Hilferding's reasoning can be found in Hobson:

At first sight it might appear that Consols and first-class railway and other stocks were open, and that the folly of the investors in bogus companies consisted in not preferring a safe 2 1/2 per cent, to a risky 5 or 10 per cent. But this argument is once more a return to the unsound individualistic view. It was doubtless open to any individual investor of new savings to purchase sound securities at 2 1/2 per cent., but, since the aggregate of such soundly-placed capital would not be increased, this would simply mean the displacement of an equal quantity of someone else's capital. A could not buy Consols unless B sold, therefore the community to which A and B belong could not invest any fresh savings in Consols. Any widespread attempt on the part of those who plunged into bogus companies to try first-class investments would obviously have only had the effect of further reducing the real interest of these investments far below 2 1/2 per cent. (Hob-

son 1894, 204f)

Hilferding considers this argumentation regarding stocks: An increase of liquid monetary capital—and with that, an increasing demand for investment opportunities—meets a steady supply of solid investments following the disappearance of fraudulent companies in 1873. This leads to a falling rate of return. Since Hilferding considers this only for stocks (and not for consols), it implies a decrease in the dividend. Unlike that of Hobson, Hilferding's lower limit is given—in accordance with Marx—in terms of the interest rate.

Also, Hobson explains the connection between liquid bank capital and productively invested capital:

Capital appears to have this fluidity when it is regarded from the abstract financial point of view. A man who has 'saved' appears to hold his 'savings' in the form of bank credit, or other money which he is able to invest in any way he chooses. But, as we have seen, the real 'savings,' which represent his productive effort plus his abstinence, are of necessity embodied in some material forms, and are therefore devoid of that fluidity which appears to attach to them when reflected in bank money. (Hobson 1894, 205f)

Therefore, capital is only liquid in an abstract form and this is how it appears in bank capital. Behind that, there are physical investments, which are not liquid. This is precisely the issue that is the focus of Hilferding's argumentation about the power of the banks against the companies. This seems to be

Hilferding's motive when defining *Finance Capital*:

I call bank capital, that is, capital in money form which is actually transformed . . . into industrial capital, *Finance Capital*. . . . An ever increasing proportion of the capital used in industry is *Finance Capital*, capital at the disposition of the banks which is used by the industrialists. (Hilferding 1910, 225)

Hilferding also uses the term "reflection":

The distinctive movement of *Finance Capital*, which seems to be independent, though in reality it is a reflection. (Hilferding 1910, 21)

Further thoughts of Hilferding can be found in Hobson's work:

The growing quantity and complexity of machinery applied to purposes of manufacture and conveyance, and to the extractive industries, is the great special fact in the narrative of the expansion of modern industry. (Hobson 1894, 6)

This gives the banks the financial processing opportunities of complex structures.

Moreover, the concentration of the economy prevents it from ruinous competition:

One well-informed writer [Jeremiah W. Jenks, who can also be found in Hilferding's library, although with a different work than the one cited here] upon the subject holds that this is the normal origin of the Trust. "With the exception of the

Standard Oil Trust, and perhaps one or two others that rose somewhat earlier, it may be fairly said, I think, that not merely competition, but competition that was proving ruinous to many establishments, was the cause of the combinations." This condition of ruinous competition must be recognized as the normal condition of all highly-organised businesses where modern machinery is applied, and which are not sheltered by some private economy in the shape of special facilities in producing or in disposing of their goods. (Hobson 1894, 137)

Branches with a big share of machines are more likely to be subjects of cartels.

Also, concentration in one sector leads to another vertical concentration:

The power possessed by a monopoly placed in the transport stage, or in one of the manufacturing or merchant stages, to 'squeeze' the earlier or less organized producers. (Hobson 1894, 143)

VI Ferdinand Tönnies

Hilferding quoted Tönnies' definition of the term "Gesellschaft" (society) from his first edition of *Gemeinschaft und Gesellschaft* (community and society) from 1887 for one of his articles in *Die Neue Zeit* (Hilferding 1904a, 106). In this article, Hilferding talks about the economic theory of Marx. The terms *Gemeinschaft* (community) and *Gesellschaft*, which was also referred to—in an economic sense—by Tönnies, can be found throughout Hilferding's article. This raises the question: To what extent is Hilferding's Marxist understanding (specifically the basic idea of *Finance Capital*—namely, the de-

velopment from an anarchistic to an organized economy) based on Tönnies' *Gemeinschaft und Gesellschaft*?

Tönnies separated the natural and organic connection between humans in a *Gemeinschaft* and the ideal and mechanical connection in a *Gesellschaft* (Tönnies 1887, 17, 233).

The theory of *Gemeinschaft* is based on the idea that in the original or natural state there is a complete unity of human wills. (Tönnies 1887, 22)

The theory of *Gesellschaft* takes as its starting point a group of people who, as in *Gemeinschaft*, live peacefully alongside one another, but in this case without being essentially united—indeed, on the contrary, they are here essentially detached. . . . Nothing happens in *Gesellschaft* that is more important for the individual's wider group than it is for himself. On the contrary, everyone is out for himself alone and living in a state of tension against everyone. . . . Nobody wants to do anything for anyone else, nobody wants to yield or give anything unless he gets something in return that he regards as at least an *equal* trade off. (Tönnies 1887, 52; these sentences are quoted in Hilferding 1904a, 106)

As the relationship of exchange becomes a paradigm of society, Tönnies connects this idea to a value theory based on work (Tönnies 1887, 54ff).

Tönnies directly refers to Marx at only three points, but the whole "theory of society" is a specific interpretation of Marx (Ru-

dolph 1991, 310f). In the foreword, Tönnies calls Marx a “profound social philosopher” (Tönnies 1887, 12), for whom “the natural, underlying constitution of civilisation (though now lost to us) is communistic” (Tönnies 1887, 13). In another paragraph, Tönnies explicitly refers to Marx when he characterizes bourgeois society as a society in which everybody needs “encyclopaedic knowledge of commodities” (Tönnies 1887, 68) and “any seller who offers the products of his own labour for sale can be thought of as a trader” (Tönnies 1887, 67). Tönnies follows Marx with the idea that an abstract relationship of exchange, profit, and good “work” are the foundations of capitalism.

Furthermore, Tönnies matches the development stages named by Marx (households, feudalism, capitalism, etc.) to his terms of *Gesellschaft* and *Gemeinschaft*. This causes them to represent specific forms of culture in a community or society and also makes exchange a decisive element.

Tönnies’ definition of *Gemeinschaft* is the basis for Hilferding’s idea of a deliberately organized production community, while the definition of *Gesellschaft* is used for his anarchistic capitalism. From *Gesellschaft*, which is defined by the exchange of goods, Tönnies moves to the topic of “money.” For him, a bill of exchange is only valid,

if the receiver is sure of being able *either* to pass it on, *or* of giving it back to the giver (or issuer). . . . It is *private money*, which Society guarantees by enforcing the liability of the debtor or his “guarantors.” (Tönnies 1887, 61)

Hilferding adopts the motif of a “guarantee

by society” (*gesellschaftliche Garantie*)—it is apparent that by this he understands, following Tönnies, a legal guarantee and enforceability (Hilferding 1910, 62).

Hilferding favors this interpretation of Marx, the emphasis on exchange, developed by Tönnies—and is later accused of a misinterpretation of Marx and an over-emphasis on the sphere of circulation (e.g. Grossmann 1929, 574).

Behind Tönnies’ construction lies a dialectical line of argument, in which the era of community is followed by an era of society. Tönnies’ projected end of society is not followed by barbarism, but instead by a “new community,” with a labor movement as its driving force (Rudolph 1991, 309). In 1919, Tönnies states that the goal of this labor movement is the restoration of the community (Rudolph 1991, 309). For Tönnies, communism means common property; in contrast socialism means for him that the state owns the property. Communism is community-based, while socialism is a kind of society (Kozyr-Kowalski 1991, 329). Hilferding’s idea of a socialist society is defined by Tönnies as follows:

In a more perfect version of *Gesellschaft* every commodity would be produced in the correct amounts and sold at its proper value by one single unified capitalistic concern which had complete foreknowledge of normal demand. (Tönnies 1887, 79)

VII Contemporary Bank Practice

England had intensively observed the German bank system before 1914. Because of this, its respect for the German financial sys-

tem, with its universal banks, increased considerably. In particular, England kept a close eye on the size and financial power of the banks and the qualifications of the personnel (Kennedy 1995, 115ff). This corresponds with Hilferding's judgments when comparing the two financial systems (Hilferding 1910, 225, 293).

But how did Hilferding, who had studied medicine, come to this understanding of the practice in German banks? As far as his library is concerned, Hilferding was initially self-taught, using textbooks. Particularly noteworthy is the work he read by Bruno Buchwald, *Die Technik des Bankbetriebes* (The Technique of Banking) 1904.

Aside from many technical and detailed descriptions of processes in the banks, Buchwald also discussed views on investment banking, which in his opinion was the major business of banks.

The view that security trading should not be classified as credit business, even in respect of business, is rightly opposed by another view, which does classify security trading as credit business, because the bank has no wish to remain a shareholder indefinitely, but wishes to grant the company, through the purchase of shares, a credit to run its business; by the resale of the shares the credit relationship is given up and transferred to someone else. (Buchwald 1904, 15—translated from German original)

This ambivalence can also be found in Hilferding's *Finance Capital*.

Aside from this German banking textbook, Hilferding's library also contained An-

glo-American textbooks about corporate finance. In his book *Modern Business Corporations*, 1906, in the chapter "Promoters' Profits," William Wood wrote:

The promoter has to create value to entitle him to profit. He provides a new or original means of making money, and makes the means productive through the development of a 'going' concern for the utilization of that means. His profit, though large, is legitimate profit. It is arrived at usually as follows. From the figures of the technical expert on the proposition, the promoter arrives at a conclusion as to the total net profits of the business when it has been developed. If he is a conservative man, he capitalizes his business on the basis of its average earning capacity with only enough 'water' to provide for increased earnings. If the proposition was one worth his efforts, it was a proposition which could be capitalized at a figure greatly in excess of what he paid for it in its undeveloped condition, and also in excess of this cost price and the development cost combined. The difference between these costs and the sum which he receives for the stock represents his profit. If options have been paid for before the property has been bought, their cost usually comes out of the promoter's profit. As a rule, the earning capacity of his proposition is such that the promoter can capitalize so as to provide sufficient working capital and sell the common stock at from fifty to seventy-five cents on the dollar, which is desirable to facilitate the sale, and still have for himself a margin of profit of from fifteen to thirty per cent of the capital stock. . . . The association of indi-

viduals in the promoter's corporation is not fortuitous, but is the result of the work of a trained business agent, the promoter, who is working for his own profit, and is earning his profit by assembling the business proposition and by securing the incorporators and other investors. (Wood 1906, 16)

Thomas L. Greene, who is also cited by Hilferding in *Finance Capital*, wrote in the same year:

The unwillingness of the average investor, individual or institutional, to put his money at any business hazard, is one of the main causes for the continued fall in the average rate of interest. Capital competes with capital for safe investments. The demand for security in loans gives the business firm or corporation its opportunity. If perfectly sound in condition and management, it can borrow its outside capital at a low rate, and so increase its own profits. (Greene 1906, 3)

Here, Hilferding's line of argument concerning the promoter's profit is set out in detail. Hilferding's achievement consists in his ability to integrate this new corporate finance literature into his Marxian theory.

VIII Robert Liefmann

The best known German-speaking contemporary economist to focus on cartels and trusts was Robert Liefmann, a former student of Max Weber. Hilferding quoted from Liefmann's writings about *Schutzzoll und Kartell* (Protective Duties and Cartels) of 1903 and *Kartelle und Trusts* (Cartels and Trusts) of 1905, primarily in the context of definitions

(Hilferding 1910, 197).

The first work was used by Hilferding to prove the whole argument concerning the topic of protective duties and cartels. It can be seen that there are hardly any differences between the view of Liefmann and that of Hilferding on their importance and effectiveness. Liefmann also took the view that protective duties have a beneficial effect on cartels and lead to cheap foreign sales (Liefmann 1903, 14ff).

Yet, for Hilferding, a different Liefmann text was of much greater interest. In Hilferding's library were found two copies of Liefmann's *Beteiligungs- und Finanzierungsgesellschaften* (Holding and Finance Companies—the editions of 1909 and 1913). It is not clear whether the edition of 1909 was available before the publication of *Finance Capital*. It is very likely that Hilferding did not read it until he was in the final phase of his studies (Liefmann's foreword in February 1909; Hilferding's foreword in *Finance Capital* in December 1909). In this case, it would have been too late for him to make use of it. But on basic points, Liefmann's text matched Hilferding's.

Liefmann developed a stage model of the economy and named the current phase capitalism, in line with Werner Sombart, "Effektenkapitalismus" (securities capitalism), whose special character was that money itself turns into capital. This happens when money is invested, which means it is lent to others, who in return purchase goods for production purposes. With the development of the banks and stock markets, the phase of capitalism emerges in which capital takes the form of securities. Furthermore, this leads to an impersonal capitalism in which real capi-

tal is mobilized by securities. An expanding economy is embodied in securities. Liefmann emphasizes the promotion of the international integration of the economy with the help of "Effektenkapitalismus."

Thereafter, Liefmann talks about the characteristics and functions of holding and finance companies as instruments of "Effektenkapitalismus." They are especially important when banks are not able to sell the new securities within a foreseeable period of time. The holding and finance companies, which Liefmann called "Kontrollgesellschaften" (control agencies), fit ideally into Hilferding's idea of a concentrating and organized economy (Liefmann 1909, 224ff). Furthermore, Liefmann made a clear distinction between holding and finance companies, on the one hand, and banks, on the other hand, since banks were involved in the credit business and the trading of monetary capital, while holding and finance companies traded securities and not monetary capital (banknotes, exchange, checks, etc.) (Liefmann 1909, 467ff). However, this separation did not exist for Hilferding. Instead, he deliberately mixed debt and equity as well as loans and bonds. For Hilferding, the business of holding and finance companies was a part of banking, and banks were shareholders of those companies.

For Liefmann, it is banks that deal with short-term financing, while the long-term financing is done with securities. Yet at the same time, Liefmann interprets the German financial system of his times as being market-based. In view of the similarities of the description of the concentration and increasing importance of the financial system, including Corporate Governance (Knetsch

1998, 230ff),²⁾ we may assume that Liefmann thought that these phenomena—as interpreted by Hilferding—were possible in a market-based financial system as well, which indicates that Hilferding's focus on the banks is too narrow and makes Hilferding's theory applicable to other distinct financial systems.

IX Conclusion

Finance Capital is, first and foremost, a Marxist work. It is shaped by the discussion within the SPD in the years of its origin, the so-called Revisionist Debate. Hilferding was close to his mentor, Kautsky, and was supported by him. *Finance Capital* adheres to Kautsky's theoretical form. Nevertheless Hilferding was at that time also an Austro-marxist and his ideas were shaped by a common intellectual development in Vienna with the other important writers of this Marxist school, especially Otto Bauer. Furthermore, less exposed socialist writers like Parvus and Theodor Kapelusz also influenced Hilferding. This integrating role of *Finance Capital* inside the socialist movement also led to some inconsistencies in Hilferding's theory, which he was unable to resolve completely and which were the basis of subsequent critiques e.g. by Lenin or Max Adler (Adler 1927).

Hilferding shows a great readiness to take up ideas from totally different theoretical backgrounds and to use them productively. Familiarity with the ideas of John A. Hobson or Ferdinand Tönnies on the development of the capitalist system clarifies Hilferding's ideas regarding banks and an organized economy. Awareness of the influence of Hobson and Tönnies on Hilferding provides the necessary background for a

deep understanding of *Finance Capital* today.

Hilferding utilized almost without modification the new corporate finance and practically-orientated bank literature in his description of the emerging contemporary phenomena in the financial sphere and used his Marxian theoretical framework to explain them.

A comparison of *Finance Capital* with the ideas of Robert Liefmann demonstrates the widespread perception among the contemporary scientific community of the power of financial institutions and the level of organization in the economy.

It would therefore be a short-sighted approach to restrict the analysis of *Finance Capital* to the context of the Revisionist Debate. It is precisely the openness of Hilferding to a wide range of influences that sets his work apart from other socialist writings of this time.

Jan Greitens

Notes

- 1) In the translation, the footnote in the original was moved into the text and Hilferding's term „Finanzkapital“ was—inaccurately—translated as “financial capital.”
- 2) This was the subject of the Liefmann/Merton Controversy (Knetsch 1998, 234ff and Rieger 1992).

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