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Competition in Transitional Processes: Polanyi & Schumpeter^{*}

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Abstract

We examine parallels and differences in the analyses of competition in processes of societal transition by Karl Polanyi and Joseph A. Schumpeter. We argue that although their understanding of historical processes differs – transformational-political vs. evolutionary-natural – the central mechanism of change is strikingly similar. We identify three spheres essential to both authors' works: the economic, the political and the socio-cultural sphere. Both Polanyi and Schumpeter describe the dominance of the economic sphere over the other parts of society. In capitalism this dominance stems from its emergence and the concept of competition. The consequence is a profound change in societal relations which distort the socio-cultural sphere via rationalisation (Schumpeter) or commodification (Polanyi). This transcends towards the political sphere and can have detrimental consequences for democracy. We capture similarities as well as differences in the respective theories, clarify the role competition plays therein and discuss the consequences for the political process. We make use of the complementarity of the theories to gain valuable insights on the interdependence of capitalism and democracy.

Keywords: Polanyi, Schumpeter, transformation, competition, democracy

1. Introduction

Karl Polanyi and Joseph A. Schumpeter are arguably two of the greatest thinkers of the 20th century. Not only did their respective works shape their fields, but they also enhance our understanding of societal change. While Schumpeter is primarily known for his concepts of innovation and creative destruction, Polanyi's ideas gained popularity in recent years thanks to his critique of the (neo-)liberal free-market ideas and their political implementation. Although less of a focus in recent contributions, both authors emphasise the processes of societal change and transition. Both present general theories of the society, starting with the emergence of the capitalist system and concluding with a prospective outlook on the political system. In the following, we argue that although their understanding of historical processes differs, the central mechanism of transition is surprisingly similar in both oeuvres.

In *Capitalism, Socialism and Democracy*, Schumpeter ([1942] 2003) presents societal change as an evolutionary process. He discusses economic as well as socio-cultural and political developments in capitalism which he ultimately expects to smoothly transition into a Schumpeterian socialism – due to inherent tendencies stemming from the economic sphere. Polanyi's (1944) *The Great Transformation*, on the other hand, offers an historical account of societal transformation culminating in fascist moves all over Europe. Societal change is portrayed as a radically transformative process that was set in motion by the utopia of an all-encompassing self-regulating market affecting political and cultural realities alike. Both Schumpeter and Polanyi focus on the rising significance of the economic sphere and identify a common factor: the incompatibility of capitalism and democracy.

While contributions specifically comparing Polanyi and Schumpeter are rare, several scholars contrast Schumpeter or Polanyi with other thinkers. For example, Schumpeter and Veblen are examined with respect to economic evolution (Schütz and Rainer 2016) as well as their

epistemological groundings (Papageorgiou and Michaelides 2016). Schumpeter's long-term economic perspectives are compared with Werner Sombart's (Chaloupek 1995) and his concepts of investment and interest are discussed alongside Keynes's (Kurz 2012). Polanyi-Levitt (2012) contrasts Polanyi's ideas and their power to Hayek's and Keynes' while Lloyd and Ramsay (2017) analyse Polanyi's and Streeck' perspectives on the role of organised labour as a countervailing force to commodification. Additionally, Maurer (2017) concentrates on Polanyi's and Weber's notion of institutions in modern capitalism.

In one of the rare contributions including both Polanyi and Schumpeter, Özel (2018) discusses the common philosophical base of Schumpeter and Polanyi (alongside Marx and Weber) in the tradition of German expressionism and emphasises the antagonistic tendencies of the political and economic sphere and the resulting instability of capitalism which is essential to all four thinkers. Harvey and Metcalfe (2004) link Polanyi's and Schumpeter's perspectives on markets and find that Schumpeter viewed the evolutionary power as originating from within the market system whereas Polanyi considered the organization of the market system as the driving force for transformation.

However, to the best of our knowledge, there has been no attempt yet to compare Polanyi's and Schumpeter's perspectives on the mechanism of societal change. In our analysis, we focus on the links between capitalism and democracy as well as on the role of competition. We primarily consider Schumpeter's analysis of late capitalism and assume the Schumpeterian mark-II-model of oligopolistic competition (see e.g. Andersen 2011) to apply. Likewise, we follow the 'hard' interpretation of Polanyi and employ a large-scale term of 'embeddedness' (Dale 2010)¹

¹ Dale (2010) discusses two conflicting interpretations of Polanyi's view on the relation of the economy, society and politics. The 'soft' Polanyi views a mixed economy with some distributive elements as 'embedded', whereas the 'hard' Polanyi demands more radical reorganisation of fundamental capitalist principles to establish a (re-)embedded market. Neither of both truncated interpretations do justice to Polanyi's prudent analysis, Dale (2010) concludes, but rather illustrate the broad range of Polanyi's intellectual influences which further result in some antinomies in his work (Dale 2010, 2014). Similarly, Cangiani (2011) detects economic as well as sociologist fallacies in the interpretation of Polanyi's theory, particularly in his concept of 'embeddedness'.

and tend to abstract from the historical context which Polanyi is describing in a post-Polanyian tradition (Holmes 2014, 2018). For the sake of clarity, we use the term ‘transition/transitional’ to refer to the dynamic of societal change common in both authors’ theories. When relating to Schumpeter’s view of different spheres engaging rather smoothly, we use the term ‘evolution/evolutionary’ in contrast to Polanyi’s consideration of societal change as a process of antagonistic (counter-)movements. The latter is termed as ‘transformation/transformational’ throughout the following analysis.

In the following, we compare and analyse Schumpeterian and Polanyian theories as presented in *Capitalism, Socialism and Democracy* ([1942] 2003) as well as in *The Great Transformation* (1944)². We do so to substantiate our claim that the mechanism of change is very similar and to answer associated questions concerning the similarities and the differences between Schumpeter’s and Polanyi’s assumptions. We additionally want to investigate what the concept of competition means for the supremacy of the economic sphere and the implications thereof. Moreover, we analyse what insights the theories offer on the dynamics and interdependencies between capitalism and democracy.

In order to answer the above questions, we compare Polanyi and Schumpeter along different categories in Section 3. Both authors present their theories of transition by describing distinct societal spheres as well as the interactions and conflicts within and between them. These ultimately lead to a transformative or evolutionary process for society as a whole. We utilise the distinction into spheres central to both theories and build an analytical framework along which to compare them (Section 2); we continue with a brief description of the emergence of the economic system in order to contextualise the origin of markets and the meaning of competition (Section 3.1. and 3.2.). Those insights are integral to the interdependence of the

² Those books of course only represent parts of the authors’ works. However, by focusing on the aspects of societal change and its implications for democracy it is appropriate to concentrate on these two. Naturally, the arguments presented can only be validated in reference to the discussed theories.

economic and socio-cultural sphere and allow us to derive certain principles regarding the stability of the capitalistic system. Both Schumpeter and Polanyi suggest that the dominance of the economic sphere is fundamental to capitalism and crucial to its stability (Section 3.3.). In Section 3.4. we analyse the impact on the political realm and the far-reaching consequences for democracy and summarise our findings. Section 4 concludes and discusses our insights.

2. Analytical framework: spheres and plasticity

Despite their diverging ontological positions, we argue that both Polanyi's and Schumpeter's theory of transition can be analysed and partly synthesised using the following framework. In both theories, society consists of roughly three spheres: the economic, political, and socio-cultural. Schumpeter talks of the economic, the political, the scientific and the family sphere whereas Polanyi explicitly only talks about the separation of economic and political life, yet he clearly references the cultural surrounding of humans, hence the socio-cultural sphere. While both authors use the term 'spheres' at some point, they do not necessarily stick to it consistently throughout their works. However, for our analytical purposes in this paper and better comparability we choose to follow this terminology.

Although all three spheres are interconnected, both authors argue for a clear dominance of the economic and we therefore conceptualise the relations of the spheres as presented in Figure 1.

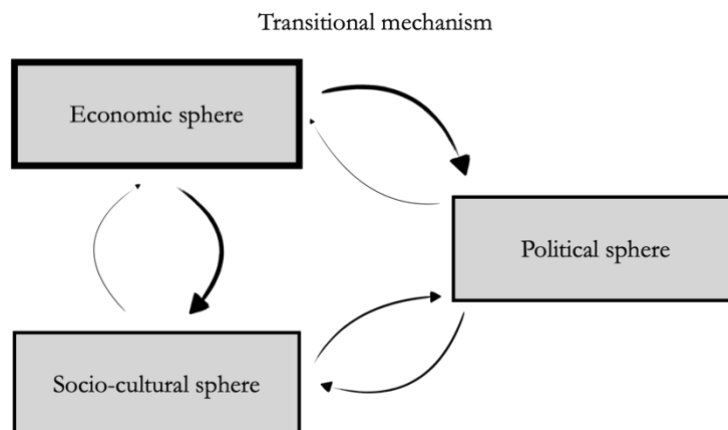


Figure 1: transitional mechanism via inter-connected spheres of society

Such a framework allows us to compare the two authors who start on different premises (transformative-political versus evolutionary-natural) in a more comprehensive way. This simplification can be neatly put into perspective permitting us to concentrate on the core mechanisms and structures of the theories.

By design, the implementation of such a framework is an abstraction from the original theories as well as a tool that necessitates simplifications. For the sake of analytical comparability and comprehensiveness, we have to accept certain limitations. However, those limitations do not weaken our argument that the three spheres are relevant in both theories with the economic sphere being dominant compared to the political and socio-cultural spheres. In a sense, such a structure is essential to capitalist societies. As soon as the dominance of the economic sector is threatened, the capitalist system stops working as intended until the necessary hierarchy is restored.

Schumpeter in his works (e.g. [1912] 1987, [1942] 2003) understands societal change as part of an evolutionary process in which in a capitalist system, the economic sphere is at centre. Society in a Schumpeterian sense can be described (as e.g. by Andersen 2011) as being comprised of several spheres or sectors: the economic, the political, the scientific and what we call the socio-cultural sphere – the latter *inter alia* includes the family where social norms are rooted. The processes of development in non-economic sectors have some analogies to developments in the economic sector, identified by Schumpeter as an alternation of static adaptation and processes of development. Even though no causal directionality can be derived from his theory, statements about the process of development and specific characteristics of the domination of the economic sphere are obtainable (Schumpeter [1912] 1987). In general, all spheres interact with each other. This forms a co-evolution of spheres – the social-cultural evolution – in which not only economic circumstances change, but also the normative conception of the economy and society. In capitalism, the economic sector is necessarily

dominant. Since rationality is a crucial component in the economic process, it influences the other spheres and changes the mode of social life by imposing a rationality dictate³ onto them. Together with the changing economic circumstances, this brings about the evolution from capitalism to a Schumpeterian socialism⁴, which is reflected in a re-organisation of societal and economic principles.

In *The Great Transformation*, Polanyi (1944) discusses the institutionalisation of what he calls a liberal utopia: the self-regulating market. He argues that the economic sphere was historically embedded in society and therefore subject to customs, norms, and moral beliefs. However, for the self-regulating market to work, regulations undermining those customs, norms and moral beliefs are needed.⁵ These regulations turn labour, land and money – although bearing no commodity character at all – into fictitious commodities enabling a self-regulating, free market “[eating] away human relations” (Hejeebu and McCloskey 1999, 288). Additionally,

“A self-regulating market demands nothing less than the institutional separation of society into an economic and a political sphere.” (Polanyi 1944, 74)

This institutional separation is also referred to as the disembeddedness⁶ of markets from society in contrast to a market that is embedded in and regulated by social norms and institutions. Competition and rationality are the core components for the market mechanism to work, but do not agree with the nature of labour, land, and money; instead, they evoke cultural

³ Schumpeter’s definition of rationality differs to some extent from other scholars at that time and relates to the methodological level rather than to an economic principle. For a detailed discussion of methodological issues in social science see Festré and Garrouste (2008) who focus on Schumpeter’s conception of rationalization in economics and his view on institutional change. They conclude that Schumpeter’s conception of rationality is both individualistic as well as holistic. See section 3.2 for a discussion on competition and rationality.

⁴ We want to emphasise that Schumpeter’s notion of socialism does not imply a total abandonment of markets or capitalist principles but is rather characterised by abandoning private property of production means, increased bureaucratisation and a government of experts formed by the elite.

⁵ Hejeebu and McCloskey (1999) analyse Polanyi’s ontological notion of the market as a concept and his integration of ethics and economic interaction in comparison to his famous predecessors, Adam Smith and Jeremy Bentham.

⁶ The term ‘embeddedness’ in our analysis refers to the more abstract definition concerning large-scale issues, as argued in Cangiani (2011), in contrast to the definition of ‘embedded’ individual decision-making, that is often used in economic sociology (see .e.g. Granovetter 1985).

degradation. Out of this tension of commodification and disembedding, the infamous countermovements arise. These political movements fight back against the pressure of the self-regulating market and the dominance of the economic sphere. Ultimately, this can result in fascist political movements and political systems as Polanyi describes for the example of Germany during 1933-1945.

As we said, both authors implicitly use some notion of societal spheres. However, they view this distinction quite differently: while Schumpeter takes it as natural and inherent to all societies and appreciates its analytical benefits, Polanyi considers the distinction of spheres as a problematic and institutionalised result of the disembedded economy. This fundamental contrast can be attributed to the authors' different conceptions of the plasticity of (inherent) attributes and behavioural traits in human nature. Schumpeter views humans' "propensity to feel and act" ([1942] 2003, 202) as well as their behaviour as formable "while the fundamental pattern underlying it [the very essence of human nature] remains" ([1942] 2003, 202). Polanyi, however, sees no such distinction between a formable and a definite part of human nature. He interprets it as given and rather rigid. Both acknowledge the interdependence of social structure and individual action. In Polanyi's view, humans are inherently collectivist whereas Schumpeter interprets human behaviour as the outcome of co-evolutionary processes of institutional change and individual behavioural traits.

Starting from this different conceptual base of human nature, both authors derive different outcomes of societal change. Moreover, the degree of determinism in transition is related to the assumed degree of plasticity of human nature. In Schumpeter's evolutionary view, individuals adapt naturally to changing circumstances. Therefore, certain degrees of freedom remain in the overall outcome of an indeterministic, evolutionary process. Polanyi, on the other hand, interprets the process of changing structures as interaction of individual needs and collective movements. Hence, the process of societal change is seen as transformative and

characterised by frictions and suffering. However, their approaches are not as exclusionary as one might initially suspect. Polanyi's rather deterministic view on transformation allows for some spontaneous elements (e.g. in the form of reactionary or emancipatory countermovements) and Schumpeter's interpretation of evolution has some destructive parts (e.g. creative destruction in innovation processes). This further highlights the insights that can be gained from a comparison of the two theories. Figure 2 depicts our analytical framework using what we call building blocks. The next chapter deal with the contextual dimensions presented in the figure.

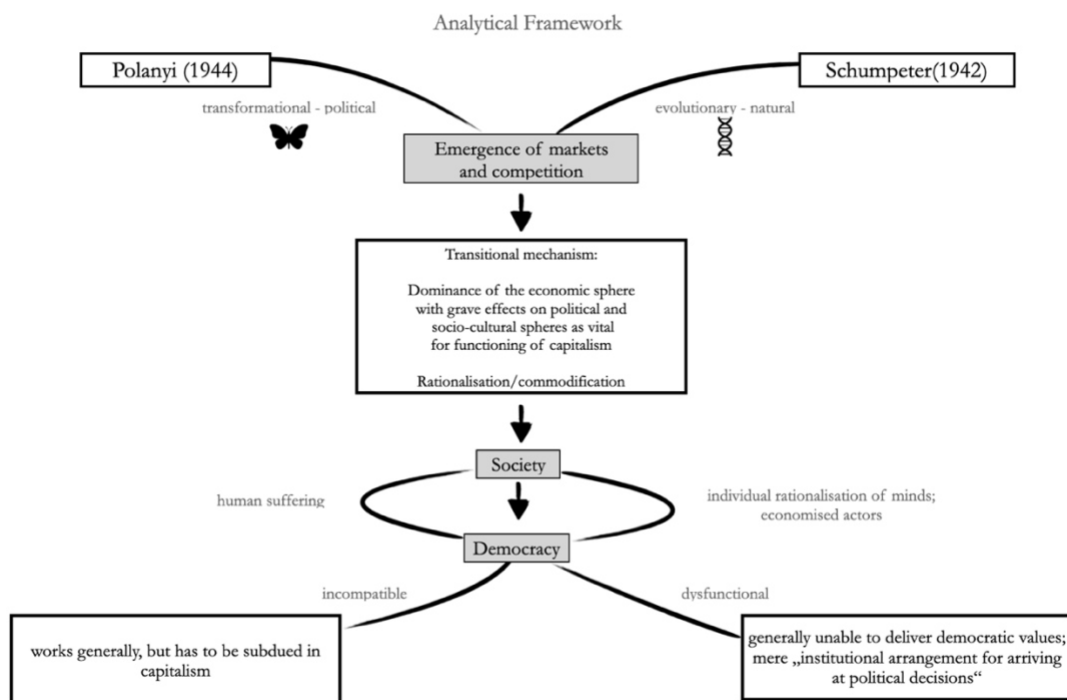


Figure 2: The Analytical Framework of synthesising Polanyi's and Schumpeter's theories on transition and societal change. The symbols at the top represent the contrasting approaches: Whereas Polanyi uses the metaphor of a caterpillar transforming into a butterfly to emphasise the fundamental element of change, Schumpeter's analysis resembles a natural-genetic process represented here by the double helix.

3. Analysis of transition

We analyse transition processes considering the following building blocks: the emergence of capitalism and the economic sphere, competition as a concept, the stability of capitalism and

democratic processes with a dominant economic sphere. Each of these acts as the building block for the next category.

3.1. The emergence of the economic system

As with the plasticity of human nature both authors emphasise different aspects regarding the emergence of capitalism. For Schumpeter, the capitalist spirit described by a rationality postulate existed long before capitalism and co-existed with other forms of economic activity until it became the dominant form of economic interaction. The industrial revolution and the subsequent rise of capitalism happened unintentionally as a result of an evolutionary development. Markets are taken as given and – because they entail competition – are necessary for Schumpeter’s argument regarding creative destruction (Harvey & Metcalfe 2004). Without competition, capitalism would not be driven to produce innovation and progress.

For Polanyi, self-regulating markets, including competition as a basic principle, have been intentionally created and institutionalised.⁷ They interfere with the prevailing functioning of society, especially considering that Polanyi disregards the narrower, formal meaning of ‘economic’ and views the economic system in a more substantivist sense. Polanyi (1944, 1992) emphasises human structures that have always existed and will always exist: specific forms of behaviour like reciprocity, redistribution, house-holding or exchange and patterns of social organisation supporting that behaviour (symmetry, centricity, autarchy and the market pattern, respectively). Likewise, markets as meeting places “for the purpose of barter or buying and selling” (Polanyi 1944, 59) and the motive of barter have preceded capitalism, but used to be just one possible mode of interaction and had no “automatic tendency to widen” (Hejeebu and

⁷ He even argues for a transformational re-interpretation of the Industrial Revolution: “The transformation to this system from the earlier economy is so complete that it resembles more the metamorphosis of the caterpillar than any alteration that can be expressed in terms of continuous growth and development.” (Polanyi 1944., 44). Polanyi’s disregard of evolutionists’ arguments becomes clear in his writings. See e.g. *ibid.* chapter 4, 45–58; and 67.

McCloskey 1999, 291). The market pattern is more specific than the other patterns and, unlike those, can create an institution with a specific, single purpose: the market. This, in turn, allows the market to be made the dominant form of interaction, such that social relations must adapt to the economic system. Polanyi portrays three types of markets: long-distance, local and internal markets. While the former two have existed since the sixteenth century, albeit in a highly regulated form, mercantilists started the endeavour to create one big internal (national) market. Consequently, the state had to intervene as Polanyi states:

“The “freeing” of trade performed by mercantilism merely liberated trade from particularism, but at the same time extended the scope of regulation. The economic system was submerged in general social relations; markets were merely an accessory feature of an institutional setting controlled and regulated more than ever by social authority.” (Polanyi 1944, 70)

Therefore, the implementation of a self-regulating market can be regarded as a fundamental and intentional transformation of organisational principles within society.

Polanyi views the economic as set and influenced by political configurations – essentially embedded. Schumpeter, by contrast, views the economic setting and the dominance of one of the spheres as the outcome of evolution, a process that can hardly be hindered nor intended. This also translates into the understanding of the transition. As Harvey and Metcalfe (2004, 9) emphasise for Schumpeter, the “source of change [is] intra-market endogenous” whereas for Polanyi, it is “market organisation endogenous”. Furthermore, Polanyi's term of ‘embeddedness’ hints to the fact that Schumpeter disregards the transitional effect of market integration on the very substance of human societies as highlighted by Polanyi (Cangiani, 2011).

3.2. Competition

The discussion above leads us directly to the key concept of markets under capitalism: competition. As already stated, competition is the main driver of change in Schumpeter's process of creative destruction⁸. Although Schumpeter considers competition to be the ultimate driver of economic growth, he also acknowledges that perfect competition was never attainable for most products and markets in capitalism (Schumpeter [1942] 2003, 78f.). The majority were shaped by some form of market power resulting from the dynamic process of creative destruction. The process of creative destruction starts at a stationary state that allows for profits once an innovation occurs. The innovation conceived by the famous entrepreneur triggers a complex competitive process based on the adaptation of new routines. New firms entering the market exert pressure as do existing firms by rapidly adapting. In this environment, firms using the old routines can persist in the competitive struggle by either adapting the new routines or by increasing productivity. Alternatively, they disappear and become a victim of creative destruction. The result is a sustained change in agents' routines and not always but mostly an increase in prosperity (Andersen 2011, 152–173).

As capitalism matures and transitions from competitive capitalism to big business capitalism, oligopolistic competition becomes central (and characterises the Schumpeterian mark-II-model, see e.g. Andersen, 2011). The importance of the entrepreneur declines, hence a new mechanism that ensures creative destruction; i.e. progress, is needed. The “constant threat” of entry and exit does the job.⁹ This concept of competition is closely linked to rationality since

⁸ Schumpeter's conception of competition changed over the years of his academic life. In the following, we concentrate on the depiction in *Capitalism, Socialism and Democracy*. Since the importance of the entrepreneur is declining in this opus so is the conception of competition as described e.g. in *Theorie der wirtschaftlichen Entwicklung* ([1912] 1987). This conception concentrates much more on competition between entrepreneurs as a struggle or even a fight (“Kampf”).

⁹ According to Schumpeter and as can also be seen by the depiction of the process of creative destruction, his concept of competition in *Capitalism, Socialism and Democracy* transcends the concept of price competition as envisaged by economists of Schumpeter's time. He argues that their analysis still rests on a stationary and rigid system and can therefore not account for the actual competition stemming from new goods and processes. He further points out that the concept of perfect competition, on which grounds attacks on monopolistic tendencies

rationality is needed to survive in the competitive struggle. Schumpeter argues that “all logic is derived from the pattern of the economic decision” (Schumpeter [1942] 2003, 122f.). It is the “inexorable definiteness and, in most cases, the quantitative character that distinguish the economic from other spheres of human action” (ibid., 123). Individuals acting rationally in the Schumpeterian sense do not imply an omniscient representative agent, i.e. that individuals are capable of accessing and processing all the information at hand and act accordingly to maximise the outcome, but “only that their rationalistic rules of thumbs are tested and selected in some core areas” (Andersen 2011, 227). Nevertheless, the importance of the economic sphere leads to a “[...] slow though incessant widening of the sector of social life within which individuals or groups go about dealing with a given situation.” (Schumpeter [1942] 2003, 122) in this rationalistic way. Schumpeter most explicitly speaks of competition transcending into the other spheres when he regards the political sphere. Competition for political leadership is defined as free competition for votes. Moreover, the rationality postulate is one of the main drivers of the change of social norms (Schumpeter [1942] 2003, 121–130). With competition and hence rationality as the defining force of capitalism’s social order, it is perceived as something positive and desirable since it enables evolution.

Polanyi neither considers the self-regulating market as natural nor does he perceive competition as something desirable. Again, his view is substantivist: competition resembles “just one form among many to organise the allocation of material goods” (Altreiter et al. 2021, 13). The reversal of the trend from local non-competitive to internal competitive markets was brought about by the “artificial phenomenon of the machine” (Polanyi 1944, 60) that consisted in “the invention of elaborate and therefore specific machinery and plant” (ibid., 78) and culminated

are launched, is pure utopia and never even existed. Additionally, the monopolies under attack were able to generate greater prosperity than were the firms under competitive capitalism (Schumpeter [1942] 2003, chapter 7, 81–86).

in the factory system. This required that all production factors involved in production be “on sale” (ibid.) and available at all times, including labour, land and money.

The motive of gain is particular to the production for markets, but profits can be obtained “[...] only if self-regulation is safeguarded through an interdependent competitive market” (ibid., 78).

A self-regulating market is characterised as able to administer production and distribution via buying and selling, i.e. by the reliance on prices, without external governance. For the smooth functioning of the price mechanism, (perfect) competition is essential: it ensures the existence of one price only (Altreiter et al. 2021). This further implies that incomes are derived from sales on the market and that no interventions should distort the price mechanism. Society, including the political and socio-cultural spheres, needs to be subordinated to the laws of demand and supply – along with the production factors, labour, land and money. Since commodities are defined as “objects produced for sale on the market” (Polanyi 1944, 75) and this definition does not hold for labour, land and money, they are referred to as fictitious commodities which are subjugated precisely because they need to be manageable for competition. Competition puts pressure on individuals and their surroundings and thus leads to countermovements. The notion of competition is therefore rather negative and perceived as an ideologically connoted design that needs intervention to be viable.

Although Schumpeter and Polanyi view the genesis of capitalism and the societal function of competition quite differently, a central mechanism remains the same: competition increasingly shapes the functioning of society. Schumpeter refers to this process as rationalisation whereas Polanyi calls it commodification.

3.3. Changing society and individuals

The feedback and influence of the economic and the socio-cultural sphere in Schumpeterian theory is administered via social norms: As mentioned above, he refers to a set of propensities to feel and act (inter alia social norms) that are subject to change through the underlying social conditions as well as an unchanging human nature¹⁰ (Schumpeter [1942] 2003). Through the lead of the economic sphere and the importance of rationalisation and efficiency social norms change and society alters its beliefs. The socio-cultural sphere “most directly reproduces and develops the norms and aspirations of the social actors.” (Andersen 2011, 225)

These norms and aspirations, and with them the political sphere, are influenced by the rationality thinking prevalent in the dominant economic sphere. According to Schumpeter, capitalism helped to promote the dispersion of “rational thought” and a “rationalistic civilisation” (Andersen 2011, 227). Situations of social life are thus increasingly met with this “rationalistic” manner which disconnects emotions and social affairs. For Schumpeter, the “economic pattern is the matrix [womb] of logic” (Schumpeter [1942] 2003, 122) as the rationalisation of society essentially leads to the rise of logic and the banishment of “metaphysical belief, mystic and romantic ideas of all kind” (Schumpeter [1942] 2003, 127). The remaining sense of duty has no “traditional basis” anymore and now directs itself towards the “betterment of mankind”, e.g. the bourgeois becoming aware of the “classwise rights” and wanting to act on them, as Andersen (2011, 229) puts it¹¹. This makes e.g. feminism an “essentially capitalist phenomenon” (Schumpeter [1942] 2003, 127)¹² that follows naturally from capitalism as it is only rational to demand equal rights when deprived of all emotional beliefs. This can also be applied to other forms of social injustice emerging from the capitalist

¹⁰ See chapter 18 “The Human Element” of *Capitalism, Socialism and Democracy*.

¹¹ See Medearis (1997, 820) who in this context speaks of the vindication of democratic values.

¹² “These tendencies must be understood “objectively”, and [...] therefore no amount of anti-feminist or anti-reformist talk or even of temporary opposition to any particular measure proves anything against this analysis. These things are the very symptoms of the tendencies they pretend to fight.” (Schumpeter [1942] 2003, 127).

system¹³. To Schumpeter, fighting such tendencies would be equal to fighting evolution¹⁴. The bourgeois class is pertinent for transition processes since it leads the other classes and thus bourgeois beliefs are of greatest importance for the overall outcome (here, Schumpeter's admiration for elites becomes evident). Combined with the evolution of the economic system towards monopolies, i.e. the economy is more profitable when centrally organised, this mechanism of rationalisation leads to socialism. Essentially, "capitalism destroys itself, not by its vices, but by its virtues." (Robinson 1943, 382)

As before, Polanyi expresses the same argument in a different, more clouded manner. Since "a market economy can function only in a market society" (Polanyi 1944, 60) that system needs to be able to "function according to its own laws", which inter alia implies a separation of the economic and political sphere. As shown above, labour, land and money need to undergo a commodification process which conspicuously resembles to the rationalisation process and transforms societal reality and socio-cultural surroundings: village structures are destroyed, leaving individuals without social shelter and protection. By comparing it to the experiences of colonisation Polanyi speaks of "cultural degradation", by which "labour and land are made into commodities, which, again, is only a short formula for the liquidation of every and any cultural institution in an organic society." (ibid., 167)

As a result of the invention of the machine, industrialists and factory owners push for the implementation of the self-regulating market. Aristocrats and workers combine forces to protect society and nature from the degradation competition and commodification signify.

¹³ Compare Schumpeter ([1942] 2003, 127): "I have pointed out before that social legislation or, more generally, institutional change for the benefit of the masses is not simply something which has been forced upon capitalist society by an ineluctable necessity to alleviate the ever-deepening misery of the poor but that, besides raising the standard of living of the masses by virtue of its automatic effects, the capitalist process also provided for that legislation the means "and the will." The words in quotes require further explanation that is to be found in the principle of spreading rationality. "

¹⁴ Nevertheless, Medearis (1997) shows that Schumpeter did not actually embrace the democratising tendencies of his time and worked up his elitist rule concept in light of the necessity to curb those tendencies. Medearis writes: "Given his definitions, "democratic" socialism could only refer to a society that happened to combine a political system of "competitive leadership" with state control of the economy." (ibid., 829)

These countermovements are typically rooted in the political sphere, namely (social) legislation protecting land and labour from commodification. In spite of this, the economic sphere clearly remains dominant and proactive as the laws passed for protection are merely reactive measures trying to alleviate consequences that are economic in origin. The political sphere acts as an intermediary although there is no change in social norms as severe as in Schumpeter's writings. For Polanyi, the unchanged human nature opposes any separation into spheres necessary for the dominance of the economic sphere and thus capitalism. Nevertheless, he acknowledges achievements such as civic liberties, private enterprise, and the wage-system that according to him "fused into a pattern of life which favoured moral freedom and independence of mind" (Polanyi 1944, 263). These are also considered worth preserving in any future society. Schumpeter, too, values these achievements of early-stage capitalism in setting the pre-conditions for a peaceful development of society.

To summarise, in both theories the socio-cultural sphere is affected by rationalisation and commodification which also impacts the political sphere (and to a lesser extent the economic sphere). In the Schumpeterian case, an evolutionary and elitist view prevails: individuals' propensities ergo their social norms are affected by rationalisation and bring about a change in attitude, i.e. they adapt to altered circumstances. In the long run, the adaptation however feeds back into the political sphere.¹⁵ The bourgeois act in the interest of the system in order to maintain the status quo but are no longer able to introduce their morals. While the political system adapts, it is unable to deliver the moral standards expected of it. Polanyi, by contrast, concentrates on transformational aspects: the economic system subjugates the rest of society, thereby destroying institutional arrangements and leaving individuals defenceless. Although

¹⁵ See e.g. Sturn (2017) for an analysis of capabilities and limits of the political sphere to cope with contemporary challenges like globalization, digitalization or ecological issues in such a co-evolutionary framework. Similarly, Sturn and Dujmovits (2018) analyse Schumpeter's concept of the state and the significance of the co-evolution of private and public spheres at different stages of development.

the political system helped the economic sphere into dominance, it now becomes the refuge and defender of working-class people. Both Polanyi and Schumpeter identify feedback loops onto the political sphere that bring about considerable consequences for the stability of the system. Those instabilities arise out of conflicts of interest stemming from the dominance of the economic sphere and principles which sooner or later jeopardise democracy.

3.4. Democracy and the political sphere

The division of society into spheres and the dominance of the economic sphere impose certain limitations on democracy in both theories. To understand the dynamics and interdependencies of the capitalist system and the political process, we have to consider the coordination of interest and the role of classes. Both Polanyi and Schumpeter view these aspects as central for the political process.

In a Schumpeterian framework¹⁶, the bourgeois class takes centre stage again. Classes are permeable on meritocratic grounds, i.e. Schumpeter ([1942] 2003) is convinced that the brightest from a working-class background can become bourgeois. This supposedly democratic permeability justifies the extensive power of the elites over the working class. The bourgeois do not only represent their own interests but are the only class able to maintain capitalist structure: they preserve the status quo by pursuing their own interest and position. In Schumpeter's opinion, the working class exclusively focuses on their own short-term interests which – as he also states – is perfectly rational. Although aware of their self-interest, the working class never develop nor express an opinion as a collective as such. Indubitably, such a balance of interests as led by one class is hardly compatible with a democratic system.

¹⁶ There has been extensive research and discussion on the democracy concept presented by Schumpeter in *Capitalism, Socialism and Democracy* (e.g. for a short overview until the 1990s see the introduction of Medearis [1997]). Scholz-Wäckerle (2016) focuses on democracy as a socio-historical process and discusses how democracy evolves along several contradictions, including Schumpeter's competitive view on democratic processes. Some examples from political science dealing with the Schumpeterian concept of democracy are e.g. Achen and Bartels (2016) and Shapiro (2016).

Nevertheless, Schumpeter ([1942] 2003) criticises the “classic theory of democracy” based on utilitarian thinking according to which democracy accomplishes to represent the “Rule by the people” (ibid., 243). For him, democracy does not deliver the values that are attached to it as it serves as a mere decision-making tool:

“Democracy is a political method, that is to say, a certain type of institutional arrangement for arriving at political—legislative and administrative—decisions and hence incapable of being an end in itself, irrespective of what decisions it will produce under given historical conditions.” (ibid., 242)

Democracy is incapable of catering to the moral standards associated with it precisely because the economic sphere has such a crucial impact on the political sphere. Schumpeter in Chapter 20 argues from a process-oriented point of view and shows that the circumstances for the Rule by the People are not given, especially not by an altered democratic system. In the short-run (the period Schumpeter is experiencing and describing), the political sphere is more and more subject to economic principles as a “battle for votes” to win the democratic election and therefore the allegiance of the people starts¹⁷. In this battle, the political parties’ only reasoning is to maintain or obtain power. The electorate, on the other hand, do not vote according to their consolidated moral beliefs but more so as a consequence of mass phenomena and persuasion, similar to a purchase based on advertisement. Competition in the political sphere results in politicians winning elections purely because of advertisement and rhetoric instead of representing the majority’s interests, moral beliefs and values. Political parties hence do not consist “of like-minded persons seeking to promote social welfare through a policy agenda”

¹⁷ Compare Ober (2017) here: According to him Schumpeter does not describe the concept of economic competition as transmitted to the political realm. He suggests that the notion of democracy employed by Schumpeter is concerned with militaristic and territorial competition. “[...] the proper analogy for competitive politics was war, not commerce.” (ibid., 488). However, as Medearis (1997) points out and as shown by our own analysis, Schumpeter's argument is not just about the concept of democracy in the political sphere but also democracy as a transitional power. That means it is characterised by overcoming feudal and hierarchical patterns that Ober argues are necessary for Schumpeter’s notion of democracy as leadership to work.

(Ober 2017, 484), but rather are “a group acting in concert in the competitive struggle for political power” (Schumpeter [1942] 2003, 283).

This, Schumpeter claims, is a suitable way to describe actual conditions in the political sphere. One of the reasons is that it “allows proper recognition of the vital fact of leadership“ (ibid., 270) – collectives do need some form of leadership. He argues that a proper coordination of interests cannot be obtained via a democratic system and hence prefers a benevolent elite¹⁸. The bourgeois class is composed of the most experienced leaders and can best represent the long-term interests of society as a whole. In the long run; democracy can thus be implemented via this benevolent and permeable elite – although it is of course debatable whether such a system can be described as truly democratic after all¹⁹. Since social norms will be altered by then, bourgeois morals can be delivered by democracy. He therefore suggests a technocratic government led by the bourgeois in his portrayal of socialism.

Likewise, the Polanyian understanding of the interest of classes is rather distinctive. He argues that – while they are merely based on material criteria, i.e. the form of their income – class has more dimensions to it and hence does not always necessarily remain constant. He also, similarly to Schumpeter, challenges historical materialism, i.e. the Marxian notion that class conflict is the main driver of historical development. Polanyi argues:

“The ‘challenge’ is to society as a whole; the ‘response’ comes through groups, sections, and classes.“ (Polanyi 1944, 160)

¹⁸ Compare Scholz-Wäckerle (2016) and his discussion of Schumpeter’s conception of elites and their function in democratic processes, where they “[...] try to reserve democracy for the republican idea through the conceptualization and interpretation of democracy as working under the same mechanics as free markets [...]“ (Scholz-Wäckerle 2016, 1005).

¹⁹ See e.g. Ober (2017) or Mackie (2009), who argues that Schumpeter’s definition of democracy is implausible as it undermines the very basic element of democracy – the existence of individual and common will. Similarly, Meadearis (1997) concerns himself with the difference and presence of the notion of an elitist democracy and the concept of democracy as an evolutionary power in the course of history in Schumpeter’s work - and thereby finds partly similar results as we do.

He sees the advent of industrial life as such a challenge. As described above, the industrialist class defended the new form of production via demanding the implementation of a self-regulating market. Workers and nobility joined forces to protect the basis of society, labour and land.²⁰ A coordination of interest is thus necessary. However, as in the Schumpeterian case, the dominance of the economic sphere results in a grave peril for democracy and eventually the basis of society. Because the economic sphere is threatening the very substance of people's livelihoods, they organise, form countermovements and protect themselves. Paradoxically, this clashes with the self-regulating market that provides for precisely that livelihood. The requirements for the self-interest-based market society to work thus make it utterly unstable.

Since capital is by definition powerful in the economic sphere under capitalism, the latter becomes the stronghold for industrialists and capitalists who make up a minority in the political sphere as they are usually fewer in terms of number. The democratic process, however, ensures that workers, who are typically stronger in numbers, control politics by building up strong unions and workers' movements. As long as no tensions are present, the conflict of interest stays latent. Once it erupts, however, the system collides. Due to the – in Polanyi's view – artificial and institutionalised separation of economic and political sphere the conflicting interests are no longer balanced by a compromise and turn into an intense conflict between the economic and the political sphere; this is problematic because either one needs the other to function²¹. This inherent instability might result in fascism – as it did at the beginning of the

²⁰ “The spread of the market was thus both advanced and obstructed by the action of class forces. Given the need of machine production for the establishment of a market system, the trading classes alone were in the position to take the lead in that early transformation. A new class of entrepreneurs came into being out of the remnants of older classes, in order to take charge of a development which was consonant with the interests of the community as a whole. But if the rise of the industrialists, entrepreneurs, and capitalists was the result of their leading role in the expansionist movement, the defence fell to the traditional landed classes and the nascent working class. And if among the trading community it was the capitalists' lot to stand for the structural principles of the market system, the role of the die-hard defender of the social fabric was the portion of the feudal aristocracy on the one hand, the rising industrial proletariat on the other.” (Polanyi 1944, 162)

²¹ “Under conditions such as these the routine conflict of interest between employers and employees took on an ominous character. While a divergence of economic interests would normally end in compromise, the separation of the economic and the political spheres in society tended to invest such clashes with grave consequences to the community. The employers were the owners of the factories and mines and thus directly responsible for carrying

twentieth century throughout Europe²². Polanyi does not consider any society as particularly prone to fascism, instead, he considers fascism “[...] rooted in a market that refused to function.” (Polanyi 1944, 248)

For fascism to assume power, the popular masses are not essential since Polanyi considers fascism a move rather than a movement, i.e., even small elite groups and tacit collaborators in power can establish fascist regimes. They succeed with their endeavour because the above-mentioned conflict surfaces and the situation becomes unbearable, leaving society paralysed²³. At the beginning of the twentieth century workers’ parties were well established and powerful enough to face industry. Industry itself prepared for the rule over the land “subverting the population from allegiance to their own freely elected rulers” (ibid., 244). Under these circumstances, market society cannot function anymore. Whenever situations threatening the self-regulating market arise, fascism surfaces in order to subvert democratic methods, paralyse labour and re-establishing the dominance of the economic sphere. Accordingly, in both theories not just the (short-term) stability of the capitalist system is important, but the

on production in society (quite apart from their personal interest in profits). In principle, they would have the backing of all in their endeavour to keep industry going. On the other hand, the employees represented a large section of society; their interests also were to an important degree coincident with those of the community as a whole. They were the only available class for the protection of the interests of the consumers, of the citizens, of human beings as such, and, under universal suffrage, their numbers would give them a preponderance in the political sphere. However, the legislature, like industry, had its formal functions to perform in society. Its members were entrusted with the forming of the communal will, the direction of public policy, the enactment of long-term programs at home and abroad. No complex society could do without functioning legislative and executive bodies of a political kind. A clash of group interests that resulted in paralysing the organs of industry or state either of them, or both-formed an immediate peril to society.” (Polanyi 1944, 243f)

²² For a comprehensive discussion of Polanyi’s thoughts on fascism and how the opportunity of fascist movements is deeply rooted in capitalism see e.g., Dale and Desan (2019). They furthermore discuss Polanyi’s thesis of socialism as a second way out of the crisis of modern society brought about by the institutional separation of economy and politics.

²³ As Medearis (1997) shows, Schumpeter in his writings is also talking about a deadlock situation arising out of the political power labour organisations assumed in the early 20th century. Schumpeter writes: “The admission of labor to responsible office and the reorientation of legislation in the interest of the working class were in a sense an adjustment to a new state of things. But, with the two exceptions mentioned [Russia and Italy], all nations nevertheless attempted to run their economies on capitalist lines, thus continuing to put their trust in an engine, the motive power of which was at the same time drained away by crushing taxation.” ([1941] 1991, 346-347) and further “The business class has lost the power it used to have, but not entirely. organised labor has risen to power, but not completely. Labor and a government allied to the unions can indeed paralyze the business mechanism. But it cannot replace it by another mechanism. [...] [E]verybody check-mates everyone else ([1948] 1991, 430).“

(long-term) stability of society as a whole. Often, however, those concepts of stability are antagonistic, yet need each other.

To summarise (see Figure 2 and Table 1), the stability of the capitalist system demands the dominance of the economic sphere and thus is essentially incompatible with democracy as being the rule of the masses. Furthermore, it is incompatible with the stability of society as a whole and hence subverted and overcome (Schumpeter) or constantly contested (Polanyi).

Comparison and summary of views

| View on matters | Polanyi | Schumpeter |
|---|---|---|
| Ontological basis of societal change | Transformational – political | Evolutionary – „natural“ |
| Advent of capitalism | Invention of specific machinery that necessitated self-regulating market; politically enforced process | Culmination of the dissemination of a rationalistic capitalist spirit; ongoing evolutionary process |
| Competition | Mechanism necessitating commodification of labour, land and money; negative, ideologically connoted design | Mechanism central for creative destruction and thus progress – synonymous with rationalization; positive and desirable |
| Changing nature of society | Dominance of the economic sphere with grave effects on political and socio-cultural sphere as vital for functioning of capitalism | Dominance of the economic sphere with grave effects on political and socio-cultural sphere as vital for functioning of capitalism |
| Stability concepts | Stability of capitalism and of society as a whole | Stability of capitalism and of society as a whole |

| | | |
|----------------------------------|---|---|
| Coordination of interests | Stability of capitalism as interest of economic sphere vs. stability of society as interest of political sphere | Bourgeois: interest in stability of capitalism as well as of society |
| Democracy in capitalism | Incompatible; has to be subdued by fascism | Dysfunctional; mere “institutional arrangement for arriving at [...] political decisions” (Schumpeter [1942] 2003, 242) |

Table 1: Results synthesised along different categories

4. Conclusion

After our analysis, we can confidently state that the central mechanism of change and societal transition is strikingly similar in both theories. The analytical framework proposed above allowed us to compare Polanyi and Schumpeter although they present extensive argumentative material and often take conflicting positions. As presented in Figure 2 and condensed in Table 1, both authors commence their analyses on different ontological assumptions and views of markets and competition. However, the transitional mechanism present in both theories works via an interdependency of societal spheres and a necessary dominance of the economic sphere under capitalism. As inherently unstable as capitalism itself, this dominance impacts individuals and – in the spirit of the respective author’s ontological basis – either leaves them and their social norms altered (Schumpeter) or unchanged with unfulfilled needs (Polanyi). Competition is a crucial and necessary concept since it induces – either through rationalization (Schumpeter) or commodification (Polanyi)– said change in the socio-cultural sphere. The same individuals also interact in the political sphere where ideally their interests are coordinated in a democratic manner. This can lead to instability via countermovements (Polanyi) or a demise of democracy due to its rationalisation (Schumpeter) which implies diverging notions of the functioning of democracy as the rule of the people as well as on the

prospects after transition. The concept of stability – capitalist and societal – helps to further improve comparability. Both authors consider not just the history of capitalism but its context in a broader history of society. This comprehensive view allows for considering democracy as non-absolutist and social constructs, e.g. classes, as variable, facilitating a critical discussion of democracy and capitalism.

Following from our framework, we can deduct significant consequences for democratic processes. Whether we accept elites as Schumpeterian benevolent considerate rulers, or regard them as Polanyian tacit collaborators, they hold significant power in a democratic system constrained by capitalism. Such observations might be helpful in explaining certain phenomena related to the failure of democratic systems and the rise in populism over the last decade or so: As Kari Polanyi-Levitt put it, the shift of power from the political to the economic sphere “constitutes a progressive erosion of meaningful democracy.” (2012, 8) This insight of if and how democracy is compromised by the interest of capital(ism) in the course of transition is enabled by a complementary analysis of Polanyi and Schumpeter.

Some prospects for future research include a detailed analysis of the conflict of interests at the societal and also at the individual level, which is rooted in the dominance of the economic sphere over society and the rationality dictate imposed by it.

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