Losing the Foundation:

How the welfare state lost its Keynesian Foundation*

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This is a preliminary draft prepared in order to stimulate discussion of the main issues. There are many rough edges that will need to be smoothed before the argument takes its final shape, and both the bibliography and the footnotes are still under construction.

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For better or worse, the modern welfare state is understood to be built on a Keynesian foundation. But what is that foundation? What exactly did Keynes have to do with the rise of the welfare state? To what extent did his ideas about the welfare state inform the way that the welfare state has been constructed in the industrial democracies?[1]

In order to answer those questions, one might look at the ethical underpinnings of Keynes's work to see if those underpinnings provide a viable justification for the welfare state. After all, Keynes came out of the Cambridge tradition, in which Sidgwick, Marshall, and Pigou had each built economic arguments on ethical grounds.[2] Each of these predecessors had developed arguments for when it was appropriate for the state to intervene in the economy and, in each case, the arguments were based on the ethical, or moral, grounds which they used to construct their economic analyses.[3] Perhaps if we understand the moral underpinnings of Keynes's theory, we can better understand his arguments for the welfare state.

This approach might seem particularly promising because of the unorthodox ethical underpinnings to Keynes's economics. Unlike many of his predecessors, and unlike the mainstream economics that emerged after the Second World War, Keynes's

[1] Backhouse and Nishizawa provides an introduction to the issues involved in trying write the history of the welfare state.
[2] See Shionoya (1991) for an excellent treatment of the relationship between the ethical theories of Sigdwick, G.E. Moore, and J.M. Keynes.
[3] Medema (2009) provides a thorough history of economists arguments for state intervention in the market economy.

economics was non-utilitarian.[4] Since the standard defenses of the laissez-faire, free market approach to economics can be construed as a form of applied utilitarian analysis, perhaps Keynes's non-utilitarian approach to economics provided him with a different moral framework that allowed him to see the value of a welfare state as a necessary bulwark for the market.

Unfortunately, as promising as it sounds to look at the non-utilitarian foundation of Keynes's work, *that part* of his work did not have a discernible influence on the rise of the welfare state. In this essay, we argue that this is true for two reasons:

1. The particular form in which Keynes's ideas became widely known (and used) in economic policy making in the modern welfare state was a "re-built model" in which the non-utilitarian foundations had been erased, and
2. While a version of Keynes's macroeconomics became widely used by policy makers in many (all?) of the postwar welfare states, the particular way that the model was used was not in the spirit of Keynes's own ideas about maintaining full-employment.

The purpose of this essay is to argue these two points and thereby to demonstrate why the modern welfare state has a foundation neither in Keynes's work , nor a non –utilitarian foundation.

<u>The non-utilitarian foundation of Keynes's economics</u>

In September 1938, while he was recovering from his heart attack of the previous year, Keynes wrote a short essay, "My Early Beliefs" to read to a group of his Bloomsbury

[4] Marshall and Pigou shared this rejection of utilitarianism but framed their ideas in ways that, in key respects, maintained the utilitarian structure.

friends who met regularly at Charleston as the Memoir Club.[5] The purpose of Keynes's essay was ostensibly to engage another essay read a few months earlier by David Garnett on the response (not favorable) of the novelist D.H. Lawrence to Bloomsbury. The essay is particularly helpful in understanding some of the early influences on Keynes's thinking, as he treats in some detail the effect on him (and his contemporaries at Cambridge and in Bloomsbury) of the philosopher G.E. Moore.

Moore's book *Principia Ethica* was published at the end of Keynes's first year at Cambridge. "[I]t's effect on *us*, and the talk that preceded and followed it, dominated, and perhaps still dominate, everything else." (1949, p. 81). Keynes's was particularly influenced by the book because he had become a member of the secret society known as the Apostles during his first year, and Moore had also been a member as a Cambridge undergraduate and often attended the group's Saturday night meetings. At those meetings, one member read a paper and the others discussed it afterward.[6] As it turned out, the group was already discussing Moore's ideas before *Principia Ethica* was published, hence Keynes's remark about "the talk that preceded" it. Likewise, they discussed Moore's work at length after the book was published, and made it a central element of membership in the group to have a "correct" understanding of what Moore had said in the book. Following the publication of Moore's book, Keynes read a series of papers to the group on themes related to it, including his first work ever on probability.

For our purposes, one of the most intriguing things about Keynes's 1938 autobiographical essay is his recounting of how Moore's disdain for utilitarianism played

[5] The essay was published posthumously in *Two Memoirs* (1949). It appears in Volume 10 of the *Collected Writings of John Maynard Keynes* in *Essays in Biography*.
[6] The paper's title was normally a question, and the discussion ended with a vote on the question. When the paper did not have a question for its title, the members formed a question from the theme of the paper.

a crucial role in the lives of the young Apostles. "[W]e were amongst the first of our generation, perhaps alone amongst our generation, to escape from the Benthamite tradition." (1949, p. 96).[7] *Principia Ethica* contains a strong argument against John Stuart Mills' utilitarianism (which it takes as paradigmatic) and dismisses Mill's ethics out of hand.[8] Moore does not deny that people experience pleasure (or utility), rather he denies that the pleasure that people feel is always "good" or desirable. In other words, he denies that utility is a sufficient basis for a theory of ethics; he denies that people will always act so as to maximize their utility, or that they would want to.

Keynes adapted both of these strictures on utilitarianism in his own work: he neither assumed that people always acted so as to maximize their utility, or that they should. Because of these two strictures, Keynes never employed utilitarian criteria as the ultimate guide in evaluating economic policy. In this sense, Keynes was far outside the mainstream in economics, where the standard assumption underlying all modeling (until quite recently) has been that people consistently employ an instrumental rationality and that they do this by maximizing their utility[9]. Keynes did occasionally speak of economic agents who used utility in their decision making, but this was never the sole or even the most important motivation. So, for instance, in the *General Theory* there are six motivations to consumption, only one of which might reasonably be conflated with

[7] This was the perception. Whether this was the reality is a different matter that we do not need to pursue here. Schultz (2004) has argued that the Apostles had more in common with Sidgwick than they acknowledged.
[8] See Moore (1903), pp. 68-81 and 104-05.
[9] This is our reason for claiming that the dominant defense of the free market is utilitiarian. Arguments centred on Pareto efficiency may dispense with the notion of summing utilities but they typically rest on a view of behavior that conforms closely with utility maximization: that was the point of much of the literature on the so-called new welfare economics of the 1930s and 1940s.

utility: “Enjoyment, Shortsightedness, Generosity, Miscalculation, Ostentation, and Extravagance.”[10]

Likewise, the two other main behavioral functions in the *General Theory*, the marginal efficiency of investment and the liquidity preference function, are not underpinned by utility maximization. In fact, both of these functions may famously be animated by animal spirits and are impossible to fully understand as a part of Keynes’s larger system without grasping that agents represented in them are driven by fundamental issues of uncertainty which can lead them to herd behaviors.

In addition to these many ways in which Keynes constructs his model in the *General Theory* without relying on utility maximization to get his essential results, he also develops a non-utilitarian means of evaluating the performance of the economy. For Keynes, the desideratum is not maximizing individual or social utility functions; it is maximizing and stabilizing the level of employment. There is perhaps some irony in this, since Adam Smith also built his argument for the social desideratum on the level of employment, and Smith was a (pre-Benthamite) utilitarian in the sense that he advocated for the greatest good of the greatest number. However, by 1936, marginalist models of the labor market had displaced the idea that the maximum level of employment necessarily connoted the maximum level of individual or social utility and so despite the similarities between Keynes and Smith in measuring social welfare in terms of employment, Keynes’s criterion for evaluating macroeconomic performance is decidedly *not* utilitarian.[11]

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[10] Keynes (1936), p.108.

[11] Smith, of course, also employs a labor theory of value, despite being a utilitarian, and so maximizing employment is also a means of maximizing the value of output. Keynes does *not* employ a labor theory of value.

What happened to the non-utilitarian basis of Keynes's work?

If Keynes had developed such an unorthodox basis for his economic theory, how and why did it fail to survive as a part of the Keynesian Revolution that swept the economics profession in the immediate postwar years? The answer to this question has two, related parts:

1. As other economic theorists developed, refined, and extended Keynes's work in the *General Theory*, they quickly and irrevocably re-built it on a neo-classical, utilitarian basis, and
2. Keynes did not discourage the early steps in this evolution of his work. He explicitly said more than once that he was not concerned with the ultimate theoretical form that Keynesian macroeconomics took as long as it conveyed his central insights about the nature of unemployment on a capitalist economy.[12]

Almost from the day that Keynes's *General Theory* was published, other economists began to re-package his work into new theoretical formulations. Perhaps the first of these came from within Cambridge when Joan Robinson (1937) re-worked the classical Keynesian-cross diagram so that the dependent variable was income, not employment. Ironically, this simple change may have been a huge step toward displacing Keynes's non-utilitarian framework since it displaced his alternative to the traditional labor market.

[12] This second point is a central argument of Backhouse and Bateman (forthcoming) where several cases in which Keynes encouraged the people who were re-shaping (or re-building) his theory on a new foundation.

Robinson's model assumed that total employment was a function of national income, but her re-working of Keynes's model nonetheless removed the alternative he had provided to the traditional neoclassical model of how labor markets determine the level of employment. Thus, Robinson's move both removed the explicit basis on which Keynes judged employment policy (the level of employment) from the basic Keynesian cross diagram and substituted in its place a variable which is often used in utilitarian models as a proxy for utility (the amount of income).

But there were soon much more substantive adaptations of his theory. Several theorists quickly joined in the effort to re-build Keynes's model on a general equilibrium basis. The most famous of these was John Hicks in his well-known article, "Mr. Keynes and the Classics" in which he developed what most economists take to be the prototype for the IS-LM model. This theoretical work blossomed quickly and was the seedbed for the neoclassical synthesis in which each function in the basic national income model was built on a simple assumption of optimizing agents who employed the instrumental rationality assumed across neoclassicism.

The great irony of these modeling changes to Keynes's work is that he encouraged several of the adaptations that led away from his non-utilitarian underpinnings. He encouraged Joan Robinson, he encouraged John Hicks, he encouraged Abba Lerner, and he encouraged James Meade. Perhaps more to the point, he made it explicit in his *public* writings after the publication of the *General Theory* that he did not care about the form on which the profession ultimately settled for expressing his insights about the instability of capitalism and the possibility of a capitalist economy coming to rest at an equilibrium with involuntary unemployment, as long as economists accepted these insights. He may have wished that the models based on his work were, like his own, non-utilitarian; but if he did harbor such a wish, he kept it carefully hidden from public view.

Although it often overlooked, one of the places where Keynes made this clearest was in his famous 1937 article in the *Quarterly Journal of Economics,* “The General Theory Employment,” in which he tried to respond to the reviews of some of his most prominent critics and so to summarize the central message of the *General Theory.*

> There are other criticisms also which I should be ready to debate. But though I might be able to justify my own language, I am anxious not to be led, through doing so in too much detail, to overlook the substantial points which may, nevertheless, underlie the reactions which my treatment has produced in the mind of my critics. I am more attached to the comparatively simple fundamental ideas which underlie my theory than to the particular forms in which I have embodied them, and I have no desire that the latter should be crystallized at the present stage of the debate. If the simple basic ideas can become familiar and acceptable, time and experience and the collaboration of a number of minds will discover the best way of expressing them. (p. 111)

This public willingness to let others determine the ultimate form in which the economics profession formulated his basic ideas reflected nicely the opinion he expressed in private (to Richard Kahn) about people who held onto old theories, even when their fundamental intuitions about the economy had changed. Complaining about how both Dennis Robertson and A.C. Pigou continued to use older models while arguing for new solutions to the Depression, he asked if they were members of "a sort of Society for the Preservation of Ancient Monuments' (*JMK* XIV: 259).

Keynes's open and tolerant attitude toward the way that his ideas were eventually captured for widespread use reflects his understanding of how the creative process worked and the high value that he placed upon creativity. Keynes's rejection of utilitarianism fit closely with the importance he placed on creativity and innovation; both stemmed from his understanding of Moore's philosophy, in which the creation and enjoyment of art were identified as among the things that were almost certain to lead to good states of mind.[13] Because he conceived of the creation of economic theory as a creative activity, Keynes never imagined that other economic theorists would not continue to improvise upon his own theoretical breakthroughs. And he would have seen this as representing a good thing, not a bad one. Ironically, then, Keynes may have been willing to see the non-utilitarian basis of his economics displaced as a result of his adherence to Moore's ethical theory. [14]

Keynes and the Welfare State

At this point, we have seen Keynes built his model in the *General Theory* on a non-utilitarian basis and that he actually encouraged many of the leading figures who helped develop the early pieces of what became the neoclassical synthesis, a version of his work that was built on a utilitarian basis. So, in some sense, the question is answered of how

[13] Moore (1903), p. 188, places the enjoyment of beautiful objects in The Ideal. He says that no one has probably ever doubted that the enjoyment of what is beautiful in "Art" is "good".
[14] See Goodwin (1999) and Goodwin (2006) for a full discussion of the role that art and ethics played in Keynes conception of his own work and how to do economics.

and why the non-utilitarian basis for Keynes work was lost in the creation of the welfare state: in adapting his work and creating the neoclassical synthesis, the profession displaced the original ethical basis of Keynes's *General Theory*. But there is more to the story than the sum of the many changes to his model that led to the neoclassical synthesis. It also happens that the particular *way* that the model was used was not in the spirit of Keynes's own ideas about maintaining full-employment.

The problem, at least originally, was not that macroeconomic theorists were not faithful to Keynes's basic insights about the nature of a capitalist economy. In the immediate postwar years, as Keynes ideas were being built into the emerging neoclassical synthesis, there was a widespread acceptance that a capitalist economy could be unstable, and hence, that it could come to equilibrium at less than full employment. Rather the problem lay in a disconnection between how Keynes believed employment could best be increased and stabilized and the ways that the architects of the welfare state believed that full employment could best be achieved. That is to say, the Keynesianism that underpinned the rise of the welfare state imagined a kind of mechanical solution to unemployment that Keynes himself did not advocate, and which led those architects to embrace the use of deficits in a way that Keynes himself never did. Understanding this difference will let us see that there are several senses in which the rise of the welfare state was not "Keynesian".

Following the Second World War, the fundamentals of Keynesian macroeconomics swept the profession and became the analytical basis for examining unemployment, inflation, and macroeconomic policy around the world. Of course, the fact that Keynesian macroeconomics became the theoretical keystone of modern macroeconomics did not mean, per se, that it had to have anything to do with the rise of the welfare state; but the reality is that the Keynesian macroeconomic model *did* play a central role in the rise of the welfare state.

But as Cristina Marcuzzo (2010) has recently argued, one must be careful in making such a statement, for in some of its most common forms the statement is actually false. For instance, one of the traditional forms of this argument is that Keynes provided the rationale for a large public sector and this is simply not true.[15] Keynes had little to say about the size of the state and he was never a vocal advocate of expanding the size of the state. Keynes's greatest concern was in securing a rate of employment that was as high and as stable as possible. Since most people associate the welfare state with large re-distributive programs in health care, family expenditure, and unemployment insurance, the direct link to Keynes is not immediately obvious. Thus, one must take care in specifying exactly what is meant when one claims that Keynes played a role in the creation of the welfare state.

Perhaps the best way to understand Keynes's influence on the creation of the welfare state would be to look at the work of Keynes's contemporary, William Beveridge, and to see the influence of Keynes's work on Beveridge's.[16] After an initial skepticism about Keynes's *General* Theory, Beveridge became an adapter of Keynesian ideas in the 1940s and he used them deftly to argue for the centrality of full employment to the effective functioning of the welfare state. Full employment was taken not only as a fundamental requirement of a just state, but it also served to maximize the amount of tax

[15] Buchanan and Wagner (1977) is the most well known source of the myth that Keynes advocated for a large state. See Bateman (2005) for a critique of Buchanan and Wagner,
[16] See Komine (2010) for a treatment of Beveridge's writing and their relationship to the welfare state. Marcuzzo (2010) provides an excellent treatment of the relationship between Keynes and Beveridge.

revenue while minimizing the number of people who would require direct cash aid from the state. Thus, to the extent that Beveridge served as a catalyst to thinking about the welfare state, Keynes's work *can* be said to have played some role in the creation of the welfare state.

Correctly articulating this link between Keynes and Beveridge has the potential to imply another possible link between Keynes and the welfare state: the use of deficit spending to sustain the welfare state. If full employment is central to the effective functioning of the welfare state, and if deficit spending is central to full employment policies, then, *ipso facto,* Keynes provided the rationale for the deficit financing that underpins the welfare state in most countries. In fact, in the popular mind, this is probably the most distinctive and clear connection between Keynes and the modern welfare state.

But while deficit financing has become the cornerstone of most welfare states, there is no historical reason to attribute this connection to Keynes, since Keynes was arguing at exactly the same time that Beveridge's work on the welfare state was coming to fruition that he believed that the "ordinary budget" for the national government should be kept in balance.[17] This fact runs most sharply against the grain of the popular idea of Keynes's work, but the simple fact is that Keynes was not a proponent of the regular use of government budget deficits to maintain employment.

Instead, Keynes believed that the way to stabilize employment was to stabilize private sector investment. In his eyes, the problem of unemployment in a capitalist system was caused by fluctuations in investment as capitalists gained, then lost, confidence in the prospects of making profits. Thus, the means to stabilizing employment was to stabilize capitalists' expectations of future profits. Keynes termed his idea of

[17] See Bateman (2006) for full discussion Keynes on fiscal policy.

stabilizing private sector expectations the “socialization of investment”.[18] Keynes believed that government expenditure could be used to this end, but it is difficult to find any support in his voluminous writings for the use of government deficits, and there is certainly no argument in his work for the desirability (or even the use) of ever larger deficits to achieve this end (much less to support the financing of the welfare state).

The key to understanding the difference between what Keynes advocated to stabilize private investment and the traditional ideas that he advocated using budget deficits to stabilize the economy is, first, to understand the way he conceptualized the government’s budget and, second, to understand his support for using the sinking fund to pay for public works projects.

Keynes was an advocate from at least the mid-1920s of keeping the government’s capital budget separate from the ordinary operating budget. Following the traditional logic of capital budgeting, Keynes argued that expenditure on investments that would generate income to pay back the amount originally invested should not be included in the ordinary budget. Thus, if an airport terminal were being constructed (or expanded), and the facility would generate user fees, there would be a stream of income that could be used to pay back the money initially used to build the terminal. When Keynes advocated public works projects, these are the kinds of projects that he advocated.

Sometimes, Keynes termed these kinds of projects “loan financed expenditure”; but, for instance, when he advocated for their use in the 1929 General Election campaign, with his co-author Hubert Henderson, in *Can Lloyd George Do It?* (JMK IX:86-125) he did not advocate the government sell bonds to finance the £250 million of public works that Lloyd George proposed. Instead, he argued that the money for the public works

[18] See Bateman (1996).

projects could be paid out of the government's sinking fund, money that had already been collected to re-pay government borrowing, but that was being held until the payments were made. Keynes's argument was that since the money in the sinking fund was being held and not invested, that it could be put to use to stimulate the economy without any harm, since the projects that it would support would eventually generate income to replace the money in government coffers. These are the same arguments that he made in (and after) the *General Theory*.

Thus, in his own context and in his own time, Keynes argued for using the sinking fund to undertake public works in the hope that if entrepreneurs and business managers came to believe that this kind of stimulus would be forthcoming when the economy slowed that they would maintain their expectations of future profitability and so prevent the swings in investment that caused unemployment. In other words, Keynes believed that profit expectations could be stabilized by well-timed, government expenditures on public works; and if expectations could be stabilized, then employment could also be stabilized.

Such a plan for stabilizing expectations and employment would undoubtedly help a welfare state run more effectively, as Beveridge argued. In such a world, fewer people would require unemployment payments and tax revenues would be higher.

But, of course, what actually happened on a global scale after the Second World War is that Keynes's name became synonymous in most industrial countries with the active use of fiscal policy to try to stabilize the economy. This was, in turn, a part of a larger phenomenon be which the emergence of the Keynesian macroeconomic model after the War provided a common framework for economic policy makers around the globe to provide an analysis of an interwar fiscal policy revolution that had happened in different countries for quite different reasons, but rarely as a result of Keynes's work. During the interwar period, many leading industrial nations had adapted fiscal policy as means of combating the effects of the Depression: for instance, Germany, Sweden, Japan, France, and the United States. In none of these countries, however, had the use of deficits been the result of politicians or economists drawing directly from Keynes's writings. Instead, the move to using fiscal policy to stimulate the economy had emerged for a variety of reasons: new political coalitions, military pressure, or independent analysis.[19]

But when the war was over, the emerging Keynesian model provided a vehicle for analyzing this new transnational phenomenon. Not only was there a common model for analysis, but the model perfectly fit the statistical categories of the newly emerging national income accounts: consumption, investment, government expenditure, net exports, and gross national product. Thus, within a few short years after the war, the models, the data, and the outlooks of many national economic policy makers became "Keynesian". And almost invariably what these policy makers were describing was how to use fiscal policy to steer the economy to its desired levels of output and employment. Thus, to the extent that a nation had used deficit spending before (or during) the war, and to the extent that war-time expenditure (and deficits) had been seen to be the cause of the improved economic performance during the war, the "Keynesian" model became the analytical basis for understanding why deficits had been used and why they had been successful.

The welfare state also emerged on a new scale after the war, as people in many industrial democracies felt that the "democracy" that they had gone to war to defend

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[19] Peter Hall (1989) is the best place to find the various histories of how industrial nations that adopted deficit spending during the interwar years. Likewise, it is the best place to see that they undertook these polices, which Hall describes as "proto-Keynesian" without direct reference to Keynes's own writings.

should include basic protections for the entire population. The feeling of social cohesion on the one hand, and the memories of the widespread deprivation during the Depression, on the other, created a new sense of optimism and hope for achieving greater social democracy. This is the moment when people came to understand the welfare state as "Keynesian".

Implicit in all this was the understanding that Keynes had not only provided the explanation for why the Depression had happened, but also that there was now a widely accepted, theoretically sound explanation that financial capitalism did not always provide full employment. Of course, the idea of capitalism as fragile and not able to always produce an optimum outcome had a long history. But Keynes's work was seen in the postwar years as offering a sound reason to believe that this was the *correct* way to understand capitalism's functioning (or malfunctioning). In this broad sense of understanding capitalism as an imperfect system that did not always provide the best outcomes, it is reasonable to link Keynes to the rise of the welfare state in a way that it is not reasonable to link him to it as an architect of deficit spending. Of course, it could rightly be objected that Keynes was hardly the only social theorist at mid-century to offer a vision of capitalism that required abandoning laissez-faire in order to maintain its viability. But he was the most well-known one and he had provided an economic framework that provided a "scientific" explanation of the limits of unfettered capital.

Conclusion

One set of conclusions to draw from the arguments in this essay has to do with clarifying the limited way that Keynes contributed to the welfare state.

Although it seems a promising prospect to ask whether the non-utilitarian nature of Keynes's magnum opus, the *General Theory,* provided a special grounding for understanding the limits of capitalism and the need for a welfare state, the answer is almost certainly not. To the extent that Keynes's ideas did influence the architects of the welfare state, they were largely in the form they took in the neoclassical synthesis, an adaptation of Keynes's work that had displaced all his non-utilitarian theorizing. And not only that, but Keynes openly welcomed these adaptations of his work in the *General Theory.* So as intriguing and evocative as Keynes's non-utilitarian ideas are, they do not seem to have played any significant role in the rise of the welfare state.

Likewise, if we take the most popular idea of how Keynes influenced the rise of the welfare state, by providing a theoretically sound rationale for deficit spending, we find that Keynes himself was not a proponent of the active use of budget deficits for any purpose. Instead, he believed in using the sinking fund to finance public works projects and he believed that this kind of fiscal policy had the potential to help stabilize the expectations of entrepreneurs and managers and so raise the average level of employment in the economy.

If we are honest, we might argue that the greatest role that Keynes played in the rise of the welfare state was the authority his name lent to the political economy that underpinned the rise of the welfare state. By having Keynes's name attached to postwar macroeconomics, there was sense on the one hand, that it was intellectually sound to believe that capitalism could not always and everywhere "provide the goods" and, on the other hand, that economist understood the economy well enough to provide good policy advice about how to keep employment at or near full employment.

But getting this picture more accurately in focus is more than just a victory for historical accuracy. As Tony Judt (2009) has recently argued, Keynes was undoubtedly the most articulate and authoritative advocate at mid-century for the political economy that underpinned social democracy and the welfare state. In this sense, Judt's argument is congruous with our conclusion.

However, to the extent that the actual mechanics of the welfare state came to rest on the misunderstanding of Keynes as an advocate of deficit spending, this history provides an opportunity to re-examine the tenuous state of social democracy at the beginning of the twenty first century. Some aspects of the crisis of social democracy derive from sources other than the welfare state's dependence on central government deficits; for instance, the population dynamics of the post-industrial democracies have created a terrible fiscal burden. But still, the dependence on deficits to finance and sustain the welfare state has created one of the largest problems of legitimacy for social democracy.

But perhaps if we look more carefully at Keynes's own ideas about maintaining full employment, we can discover a different ground for re-thinking the management of the welfare state. Of course, this may mean a quite thorough re-working of our ideas of the policies that are necessary to make the welfare state viable. Likewise, this re-examination portends a thorough re-thinking of the connection between capitalism and social democracy. But if social democracy is important, then this re-examination must be worthwhile. For the understanding of that we have worked under for the last sixty years does not work anymore and if we cannot find a new way to conceive of supporting and financing the welfare state, social democracy does not have a bright future.

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