Business Enterprises and Business Cycles (or a Microfoundation of Business Cycles)

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1 Introduction

The penetrating theme in heterodox theories of business cycles is that cycles are endogenous or, in other words, prosperity is the cause of depression. Such a theoretical viewpoint is based upon the fact that business cycles are in its nature dynamic, evolutionary, and historical; fluctuations moving through historical time cannot be analyzed from a static viewpoint trapped in the equilibrium analysis. That economic activities and their outcomes are constantly fluctuating due to inherent factors of the capitalist economy leads to a range of claims that the capitalist economic system is unstable (Keynes 1936; Schumpeter 1927; 1928; Minsky 1986b), a society dominated by business institutions is prone to disturbances in a chronic manner and material welfare of community is deteriorated (Veblen 1904; 1921), by its normal functioning the system is moving toward a secular stagnation (Baran and Sweezy 1966; Steindl 1972), or the class-based capitalist system is destined to collapse (Marx 1990; Marx and Engels 1848; Gillman 1965).

While they are connected through cross-influences over time in broadly defined heterodox economics, above mentioned approaches shed different lights (and shades) on business cycles and, more fundamentally, the operation of the capitalist economy. It is hardly possible to illustrate all important theoretical and practical implications drawn from them. What is picked-up and scrutinized in this essay is the relation between the business enterprise and business cycles. This is because business activities, whether they are routine or innovative, lie at the heart (or root) of business cycles in the capitalist economy. The goal of this essay is to point out the role of capitalist business enterprises in the context of business cycles—that is, heterodox microfoundations of business cycles.

Main arguments developing in this essay are,
1. business cycles reflect both the instability of the capitalist economic system and the instability of the capitalist social order,
2. macroeconomic policy is designed to protect the existing capitalist order by reducing the instability of the system, therefore,
3. a theory of business cycles goes beyond the economic domain—it is a social issue. In addition,
4. Microscopic investigations of business enterprises and business cycles shed light on the instability of the order.

In the following section, two widely received theories of business cycles (à la Schumpeter and Minsky) will be critically examined in terms of the concept of instability. Section 3 will develop a microfoundation of business cycles with the emphasis on the business enterprise and its decision making mechanisms. Section 4 concludes the essay.

2 Rethinking Instability

The gist of heterodox theories of business cycles is the vantage point that capitalist economy is inherently unstable. The significance of this perspective is that 1) the cause of instability lies in the nature of capitalism, 2) the instability cannot be avoided or overcome unless the capitalist economic system and the capitalist social order change fundamentally, and thus, 3) the life attached to the capitalist economy is vulnerable. What is really meant by instability in this regard is not the *irregularity* in statistical observations, but the *unreliability* of the capitalist market principle as *modus vivendi* and the *vulnerability* of individual life and individual business enterprises.

Heterodox analysis of business cycles thus requires a deeper inquiry into the structure, mechanisms, and agents embedded in social relationships than a study of numerical representation of economic activities. Heterodox analysis may end up with reformative and egalitarian policy recommendations (if the current system is to be saved) or transformative insights including the changes in habits of thoughts and vested interests or the capitalist order.

What seems most important to the present writer is to address the limitations of the frameworks received by contemporary heterodox economists in order to clarify what they are missing in dealing with business cycles.[1] To proceed this we will rethink an essential concept in heterodox theories—instability.

2.1 Schumpeter's Instability Thesis

In his article, "The Instability of Capitalism," Schumpeter distinguishes the capitalist economic system from the capitalist order. The former is, compared to other economic systems existed before, "characterised by private property (private initiative),

[1]Orthodox accounts of business cycles are not a concern here for the reason just stated. To iterate, as many heterodox economists unraveled, orthodox economics occupied with methodological individualism, mathematical formalism, and equilibrium in logical time are not able to explain the structured reality which are ever changing (see, for example, Veblen 1909; Lawson 2003; 2009; Henry 2009a).

by production for a market and by the phenomenon of credit" (Schumpeter 1928, 362). And the latter is the institutional framework (i.e., social, cultural, and moral conditions) that surrounds the economic system (ibid. 363). From a evolutionary perspective, Schumpeter sets forth that the capitalism eventually evolves into socialism through entrepreneurial capitalism and, then, bureaucratic/organized/trustified capitalism (Schumpeter 1928; 1942).

Like such radical evolutionary thinkers as Karl Marx and Thorstein Veblen in particular, Schumpeter's instability-of-capitalism thesis encapsulates that capitalism is *just another system and order* that organizes the way of life and the social provisioning process. That is to say, any human-made system and order is not natural, not universal, and not eternal, while the ruling class promotes "the view that what exists is not only "meek, right, and salutary," but normal" (Henry 2009a). In realty, *both* the capitalist economic system and the capitalist order, like others existed before, are inherently unstable. Changes in the existing system and order depend on social relations between the ruling class (i.e. the business enterprise and the state) and the ruled class (i.e. the working class and the dependent class). In this line of reasoning it is also implied that any variant of capitalism like welfare capitalism in the Western society after the World War II is inherently unstable, although social unrest and conflict can be placated by the state's welfare policy. So welfare capitalism was replaced by neoliberal capitalism. This historical change reflects the increasing dominance of the capitalist class over the ruled class. Furthermore, as we have been observing recent years, neoliberal capitalism has shown serious economic and social instability.

Schumpeter's vision is distinctive from other heterodox thinkers who place social conflicts at the root of radical social changes. Arguably, we may classify them into two groups: pessimists (e.g. Marx, Veblen, Kalecki) and optimists (e.g. Keynes, Schumpeter, Minsky). What is interesting in this grouping is that while pessimists are in the main concerned about the instability of the capitalist order, optimists lay stress on the instability of the economic system. Such a difference lies in the recognition of social conflicts underlying the capitalist economy embedded in the capitalist society.

In the Schumpeter's thesis, while antagonistic class relation disappears, the engine of evolution lies in the material success of the capitalist economic system and the cultural contradiction of the capitalist order (that is, the contradiction between radical individualism and the coordination of the society) (Schumpeter 1928; 1942; Caeldries 1993). The substitution of cultural conflicts for class/social conflicts makes Schumpeter's thesis weaker and untenable especially in the context of the instability of the social order. For example, Schumpeter conceived the shift of power from the private sector (the business enterprise) to the public sector (the state) as a change in the order. In reality, however, both the business enterprise and the state pursue the same goal; the stability of the economic system and the social order. This goal is achieved only if those two dominant agents representing the capitalist class can cooperate successfully with each other. So one requires the other for the sake of survival and the protection of the vested interests and the social order. Radical changes in the social order (e.g. from feudalism to capitalism or to socialism, or from monarchy to democracy) were achieved as a result of the struggles between classes or between topdogs and underdogs. The power transition from the private sector to the state, or the other way around in the era of neoliberalism, should be understood as an elaboration of capitalism so as to maintain the existing order. It can thus be said that Schumpeter's instability thesis does not capture the gist of historical transformation of the order, since the essence of capitalism—class conflicts and social discords—is eliminated from the scene.

With the absence of the notion of hostile class relation, Schumpeter worried primarily about the loss of dynamics designed and managed by entrepreneurs. Therefore, unlike Marx and Veblen who envision a society organized through the interests of the working class or the efficient engineers (e.g. Marx and Engels 1848; Veblen 1921), Schumpeter desires capitalism be organized by entrepreneurs who are capable of innovating the economic process in a more efficient way. Schumpeter sets forth that

> the instabilities, which arise from the process of innovation, tend to right themselves, and do not go on accumulating. And we may phrase the result we reach in our terminology by saying that there is, though instability of the *System*, not eocnomic instability of the *Order*. (Schumpeter 1928, 384, original italics)

From a radical perspective à la Marx and Veblen, an innovation—that is, a deliberate action by knowledgeable entrepreneurs—protects the existing order as well as stabilizes the economic system by creating wealth *for* the business enterprise *qua* the capitalist class. And the innovation is the source of economic 'progress' designed *by* the business class (Schumpeter 1927, 305). What is significant in Schumpeter's theory of business cycles is that the capitalist order is not necessarily unstable as long as there is continuous efforts by entrepreneurs to reduce the instability of the system. So while Schumpeterian entrepreneurs play an essential role as "as the dynamic carrier of progress who performed an invaluable function in propelling an economy's foward momentum" (Barber 1996, 37), the consideration of social conflict disappeared in his dynamic analysis of capitalism. Moreover, a business cycle as an endogenous transition between a boom to a depression is a result of normal business activities and is nothing but a movement from one equilibrium to another equilibrium (Schumpeter 1927, 294). In this respect, Schumpeter is more leaning toward Walras than Marx.[2]

In sum, with apparent limitations in approaching the evolution of capitalism, Schumpeter's instability thesis throws some light on the relationships between economy and society, between the economic system and the social order, and between fluctuation (i.e. instability of the system) and transformation (i.e. instability of the order), which lend themselves to the accounts of business cycles. A particular economic system organizes individual and collective economic actions given the constraints set by legal, moral, conventional, and cultural institutions of society. Since capitalism is sustained only if economic/material success continues, the moral (and also natural) basis of the society becomes inimical to the very economic success. The economic system and the social order (or economic and social principles) become contradictory. Conflict may be held in check temporarily if social forces are able to or the state is, although it is unlikely, willing to control the success of private business enterprises. Similarly, economic fluctuations may be held in check if the state exercise its political, legislative, and administrative power to reduce the instability of the system.

It however does not mean that both social conflicts and business cycles can be avoided. Only the transformation of capitalism (or the radical changes in the capitalist order) can resolve conflicts and instabilities built-in to capitalism. Business cycles thus reflect both the instability of the system and the instability of the order. The point that should be stressed here is that the distinction between the system and the order has an important analytical merit in inquiring into business cycles. By this distinction, we are able to separate the fluctuations in economic variables from the changes in the socio-economic order. Heterodox economists should not constrain themselves into the instability of the economic system, if they are to provide deeper and extensive analyses of capitalism.

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[2]Note that Schumpeter 'admired' both Marx and Walras. In the Preface of *Ten Great Economists: From Marx and Keynes* (1951), Elizabeth Boody Schumpeter remarked that:

> For Schumpeter the progress of economics as a science depended on vision and technique. As he admired Marx for his vision of the economic process, he admired Walras, whom he met only once, for his pure theory....Marx and Walras were poles apart: the one attempted a logical explanation of economic change; the other gave us a 'theoretical apparatus which for the first time in the history of our science effectively embraced the pure logic of the interdependece between economic quantities' "(p. ix).

2.2 Minsky's Financial Instability Hypothesis

In inquiring into the instability of capitalism from a heterodox perspective, Minsky's financial instability hypothesis should be mentioned since it captures the gist of Keynes's macroeconomics (especially, the instability of investment demand that is the cause of systemic instability) and it is what contemporary Post Keynesians have been relying on in the account of financial crisis. Since it is well developed and interpreted by himself and other Post Keynesian scholars (see, for example, Minsky 1982; 1985; 1992; Wray 2009), it is needless to repeat Minsky's hypothesis. What is more interesting here is the limitations of the financial instability hypothesis in light of the instability and the evolution of capitalism.

Following the discussion explicated above, we can argue that Minsky's hypothesis is only about the instability of the economic system, especially, the financial system. Minsky, insofar as the hypothesis is concerned, does not touch the instability of the capitalist social order. For Minsky (following Keynes), the source of systemic instability is volatile entrepreneurial expectations and uncertainty, which lead to unstable investment demand that is mainly dependent upon the financial sector. So the hypothesis concludes that "the processes which make financial instability are an inescapable part of any decentralized capitalist economy—i.e., capitalism is inherently flawed" (Minsky 1982, vii). Such instability does not necessarily lead to disturbances or unrest of the capitalist society; not even necessarily to "It" (that is, a failure in the capitalist system like the Great Depression), if "the institutions [i.e., the big bank and the big government] and interventions that can contain the thrust to financial collapse and deep depression" (ibid., viii). It is implied that the capitalist order is (to be) stable, while the capitalist economic system is fragile. This conclusion is consistent with the theoretical and political perspective shared by Minsky and other 'liberal' Post Keynesians.[3]

In spite of its relevance in dealing with instability in the economic system, Minsky's hypothesis lacks some essential elements constituting the provisioning process under capitalism. Firstly, similarly to Schumpeter's vision, the antagonistic class relations takes no place in Minsky's hypothesis (Crotty 1980).[4] In consequence, it is hardly possible to take into account social conflicts and arrangements driven by and leading to economic instability. Not to mention, the instability of the capitalist order is not a concern.

[3] For the discussion of diverse political positions within Post Keynesianism, see Jo (2009).

[4] In fact, class relations play little role especially in Fundamentalist Keynesianism. It is uncertainty and money that set the tone for the theory of monetary production economy and its instability.

Neither do they treat the capitalist state as a capitalist class segment. An immediate consequence is that the benevolent state (represented by the big bank and the big government) serving the public interests, rather than serving the vested interests of the ruling class is assumed in their economic theories. As a further result, more often than not an egalitarian economic policy is promoted, rather than attempting to change the structure and the order which lend themselves to the problem at hand. Radical perspectives in Post Keynesianism disappeared. In this regard, there is no fundamental difference between Post Keynesian policy and (mainstream) Keynesian policy—both are primarily concerned about the stabilization of capitalism.

Such is not to say that the instability hypothesis or an egalitarian policy is to be rejected, but to say that we need to recognize its limitations when it comes to the instability of the capitalist order. The dominant order of the capitalist society is the representation of the interests of the ruling class—especially, business enterprises and the state. Individually and collectively, capitalists exercise their power to maintain the existing order. However, the market-based provisioning process does not automatically find its equilibrium position. Rather, markets tend to destabilize/destruct themselves (the system) and society (the order) (Veblen 1904; 1921; 1964; Polanyi 2001). To protect the market system and the capitalist social order, not only the conflict between the market and the society, but also the conflict between classes should be attenuated. That is, the interdependence between the instability of the economic system and the instability of the capitalist order should be taken into account as an essential part of a capitalist cycle theory.

Another theoretical shortcoming that contributes to the limited explanatory power of Minsky's instability hypothesis is the accounts of the business enterprise. Indeed, Minsky's hypothesis sheds ample light on theoretical and practical implications of the relationship between business enterprises and the financial stucture. However, business enterprises operating in the real sector play a passive role in the development of endogenous business cycles. In rejecting neoclassical theory of the profit-maximizing firm, Minsky argues that the business enterprise is to be looked through its balance sheet that is relevant to the explanation of the survival conditions of the firm (Minsky 2004, Ch.4). Moreover, the market structure and its effect on firms' investment-finacing behavior is revealed in the balance sheet. In this respect, Minsky notes that

> [t]he structure of the balance sheet of business firms will reflect the psychological attitude toward risk taking. Balance sheets which contain large cash margins and a large volume of government bonds and other fixed vlaue assets which are essentially unrelated to the firm's production process indicate a cautious attitude toward risk bearing whereas the

ownership of no assets not immediately relevant to the business of the firm indicate a more adventuresome attitude toward risk. (Minsky 2004, 98)

In line with Marshallian–Keynesian–Schumpterian insights,[5] Minsky's theory of the firm as a basis of his instability hypothesis links the real sector to the financial sector with an emphasis on the latter (Delli Gatti and Gallegati 1997; Toporowski 2006). The business enterprise's investment-finance decision is subject to the financial markets. As the financial instability hypothesis manifests, it is the financial institutions that controls the business enterprises operating in the real sector—i.e., the financial theory of investment. The systemic instability develops as a result of financing decision made in the financial markets in which the level of investment is determined by supply and demand prices of capital assets (Minsky 1985, 30).

By constraining the business enterprise and its activities into the balance sheet, the financial instability hypothesis fails to take into account well articulated Post Keynesian/heterodox theories of the business enterprise based upon a set of empirically grounded principles such as the administered price doctrine, cost-plus pricing principles, strategic decision making under fundamental uncertainty and in historical time (Eichner 1976; Lavoie 1992; Lee 1998; 2009; 2010; Dunn 2001; Jo 2007). Such principles expound not only the hierarchical-organizational structure of the business enterprise, but also its role representing social relationships underlying the capitalist monetary production economy.

From a heterodox microeconomic perspective, business enterprises, especially corporations, exercise their economic-political power to contain vulnerability of themselves (micro-instability) as well as instability of markets and the system as whole (macro-instability) in order to survive and grow over time. Closely tied pricing-financing-investment-production-employment decision mechanisms at the enterprise level imply that the business enterprise does not passively take prices (of intermediate capital goods, of surplus goods, and of financial assets) determined in the markets, but actively makes prices so as to achieve its long term goals—survival and growth. Moreover, the business enterprise, on the one hand, organize themselves in various forms such as trade associations and cartels for the sake of governing the individual markets and, hence, of reducing micro-instability. On the other hand, the state (as the administrative, legislative, and judicial organization) regulates markets in primarily order to protect private enterprises from various uncertainties and

[5] According to Toporowski (2006), Minsky adopted Kalecki's theory of profit. But it is inconsistent with Minsky's Keynesian-Marshallian monetary analysis. Minsky did not pay attention to this. The Keynesian/Marshallian theory assumes a representative firm. Kalecki's theory assumes differing degrees of monopoly which influence largely on individual firm's behavior.

instabilities (Prechel 2000; Lee 2002; Henry 2007; Jo 2009). So the reduction in both micro- and macro-instability is necessary to preserve the *status quo* and the capitalist order.

The evolution of capitalism moving toward the increasing dominance of financial business enterprises since 1970s, or what Minsky named the "money manager capitalism," has increased both micro and macro instabilities of economic system. At the micro level, financial innovations like creating new financial derivatives made financial enterprises possible to gain 'bonanza.' The financial innovation is, unlike the Schumpeterian-industrial innovation, speculative rather than productive in its character (Minsky 1986a, 349). In consequence, the vulnerability of industrial enterprises as well as the instability of the economic system as a whole have been rising since industrial investment and production becomes more variable (Wray 2009). As Cornhels remarks from a Veblenian perspective, "financial empires are created at the expense of real production of valuable goods and services and sometimes the survival of the corporation itself" (Cornehls 2004, 39).

Such an evolution in the financial structure was possible because the state the private enterprises together dismantled regulations that would otherwise prevent destructive competitions between business enterprises for the sake of short-term monetary gains. Obviously, the detrimental consequences of those actions were not expected before the crisis. What is expected after experiencing a serious economic crisis is enterprises' demands for market regulations through the state's legislative and administrative process to prevent individual markets from collapsing. The state is willing to and able to support enterprises' requests. So systemic instability is in check by saving business enterprises. This is precisely consistent with the capitalist order.

Given this larger picture depicted by heterodox thinkers, financial instability is only a part of entire problems inherent to capitalism. It shall be further detailed later that although the business enterprise in conjunction with the capitalist state attempts to stabilize markets, the instability of the capitalist order does not disappear. Furthermore, the capitalist economic system is unstable as long as provisioning process is controlled by business enterprises and the state. In this light, fundamental uncertainty as a cause of the volatile economic activity is not a substitute for class/social conflict which lead to the instability of the capitalist order. What is necessary is the consideration of both elements in illustrating the evolution of capitalism. This point shall be developed in the following section.

3 A Microfoundation of Business Cycles

The discussion on the instability of capitalism leads us to rethink the theoretical framework of business cycles. While the instability of or the cycles of economy as a whole is well explained by heterodox macroeconomic analyses, the fact that such an instability is the outcome of activities undertaken by the dominant agent is not well theoretically developed. For the sake of the latter analysis we need to reverse the conventional causality running from macro to micro. Such a framework may be called as heterodox microfoundations of business cycles which is paying more attention to the roles of the business enterprise.

For example, Veblen comprehensively developed his theory of business cycles *qua* the theory of modern welfare in *the Theory of Business Enterprise*. Later Michal Kalecki (1954; 1971) and few Post Keynesian economists such as Alfred Eichner (1976; 1987) and Frederic Lee (1998; 2007; 2009; 2010) developed a framework that integrates micro and macro analyses.[6] In what follows I will elaborate microeconomic accounts of business cycles with an emphasis on the underlying social relations and the instability of capitalism.

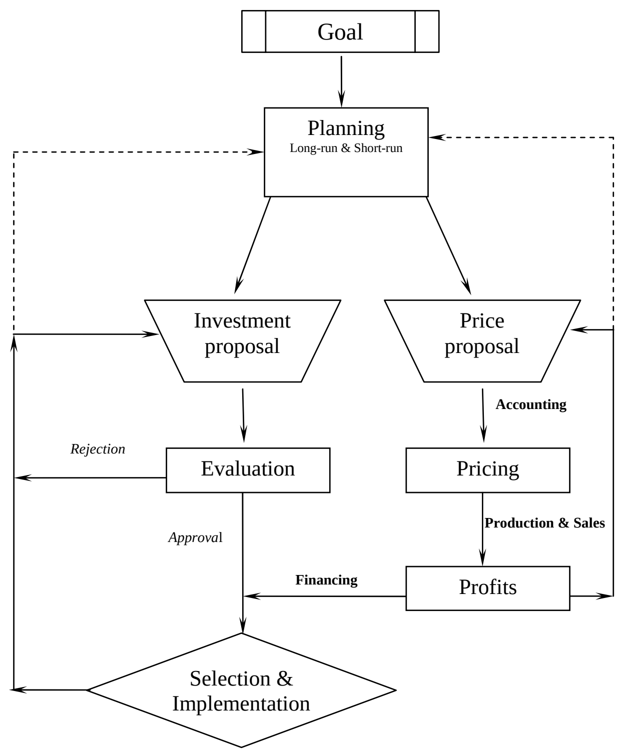
3.1 The Business Enterprise in the Monetary Production Economy

From a heterodox perspective, the business enterprise is viewed as an organized going concern operating in historical time with a goal of survival and growth. Its activities in the context social provisioning process given the institutional set-up and the industrial structure are organized so as to achieve this goal. However, the goal is not always achieved as expected due to radical uncertainty, even though the business enterprise uses resources wisely or innovates its production and slaes processes. Thus important business decisions are made strategically so as to reflect the internal-hierarchical structure of the business enterprise as well as social relationships with other agents in the society. Business activities such as employment, production, pricing, financing, and investment are socially, historically, and institutionally contingent. In particular, historical time and uncertainty play an essential role in making decisions in the sense that business activities are undertaken with an expectation to increased monetary profits and such an expectation is not necessarily fulfilled. Hence actions flow sequentially and procedurally. To illustrate decision

[6]See (Jo 2007, Ch. 2) for an extensive survey on heterodox microfoundations approaches. For a critique of the heterodox microfoundations project, see King (2008).

making procedure within the business enterprise, consider a following figure that illustrates the key relationship between pricing and investment through financing.

Figure 1: Pricing, Financing, and Investment within the Business Enterprise



To achieve the goal (i.e., growth and survival) investment should be made based upon both short-term (1-2 years) and long-term plans (2-5 years). The latter includes, but not limited to, merger and acquisition, expanding business to a new market and to a new geographical place since it is associated with a longer time horizon of physical capital and financing conditions, while the former deals mainly with routine business activities (Barna 1962; Rosenbelt 1980).

A proposed investment project according either to a short-term or a long-term plan is evaluated by top management and the board of directors (if the project is significant) or by middle/lower management (if it is routine). Only a project that is expected to generate a target cash flow and that is consistent with financing conditions will be approved. An expected cash flow may be fulfilled by setting the price strategically by marking-up over costs related with production (direct material and labor costs) and with the managment of the enterprise (overhead costs and depreciation). Net profits (after paying taxes, dividends, and debts) are the primary source of financing investment. Additional external funds may be used if the expectated profit flow exceeds the perceived risk of using external funds. That is to say, external financing is a secondary option and hence the received fact that investment is manly a function of the rate of interest has little relevance during the normal business cycle (Kalecki 1971, 105-6; Eichner 1976, 86-8; Baran and Sweezy 1966, 18; Lee 2002; 2010).

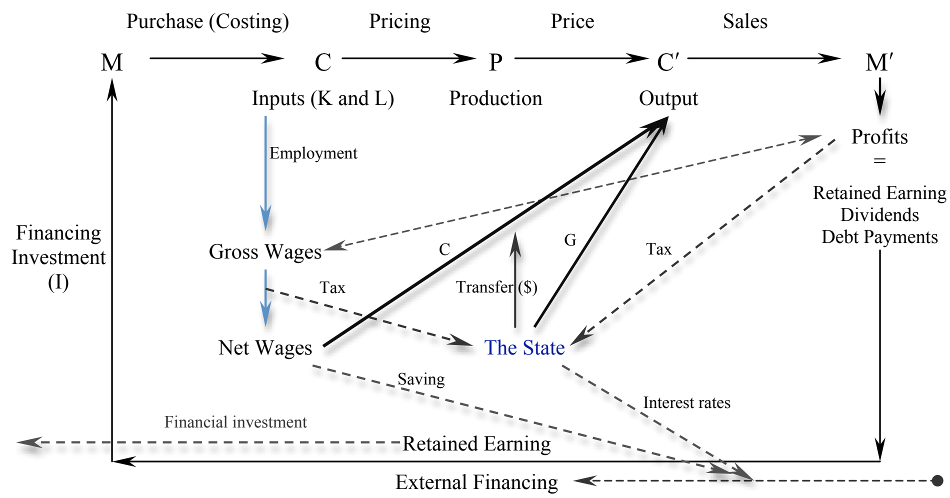
In sum, at the enterprise level investment and pricing decisions are tied through financing decisions. Strategically determined prices are supposed to reproduce the enterprise rather than to clear markets. And since product prices are set given positive profit mark-ups and/or wage rates,[7] and technical conditions that enables the enterprise to use a fixed ratio of inputs (that is, input pricing coefficients found in the input-output table of the economy), it is the social system of production as a part of social provisioning process that determines product prices (Lee 1998; 2010). A negative disturbance in the social system of production at any given point of time would tend to destabilize prices and investment. However, business enterprises, often with the help of the state, make every efforts to stabilize prices. Otherwise, a disturbance in the economic system would amplify itself through the systems of price, investment, and production. The explanation of investment as a cause of business cycles can be furthered by taking into account the monetary production economy. The following figure of a simple monetary production economy extends our discussion into the macro-level.

First of all, the figure clearly shows that the business enterprise is a socio-economic entity which is in charge of producing goods and services and hence is the material basis of social provisioning process. The dynamics of the monetary production economy is the outcome of the business activities or, as Veblen puts it, the business enterprise is "the directing force which animates this framework [i.e., the material framework of the capitalist society]" (Veblen 1904, 1). The key to the reproduction of the entire system is business investments.

Both the state and the working class are dependent upon the business enterprise *qua* the capitalist class in different ways. The state directly takes part in the formation of effective demand by purchasing final goods and services (i.e., surplus goods),

[7] There is no clear-cut explanation how profit mark-ups are determined at the enterprise level. It is widely received by Post Keynesians/Kaleckians that the degree of monopoly and the profit mark-up are positively related (Kalecki 1971; Steindl 1972; Baran and Sweezy 1966; Eichner 1976). However it is not easily supported by evidence. Rather, such factors as conventions, tradition, fairness, and competition are found significant in many case studies (Lee 1998, 226). Similarly, wage rates are, on the one hand, determined at both enterprise and industry levels through the bargaining process. On the other hand, wage rates reflect society-wide standard and enterprise- and industry-specific conventions (Eichner 1976; Lee 1998).

Figure 2: Monetary Production Economy



by increasing purchasing power of the working class through welfare transfers (in cash and in kind). Indirectly, the state may affect business investment by setting taxes (e.g., corporate tax and sales tax). Following the principle of effective demand it should be noticed that taxes are generated by actual expenditures made by households, business enterprises, and the state. That is, the causality runs from expenditure to tax revenue, rather than the other way around. For the sake of stabilizing the capitalist system, therefore, the state actively engages in the social provisioning process as the state money creator who commands private agency to use the state money in all economic activities, as the taxation authority who redistributes incomes, as the public consumer who purchases surplus goods, and as the welfare purveyor who channels the state money into working/dependent class households. Without such activities, the effective demand of the economy would fall significantly short of sustaining the economy as a whole. Hence the stability of the economic system would be jeopardized.

The working class is also an essential part of the social provisioning process in way that the survival and welfare of working class households are dependent upon the business enterprise as the employer and the state as the welfare purveyor. Since it is the capitalist class as whole that commands resources (including labor power) and the business activities are based upon volatile expectations of cash flows, the life of workers are vulnerable as well. In other words, the capitalist market mechanism does not lend itself to the welfare of the working class. Non-market activities such as welfare transfer and public works (or welfare capitalism in general) are necessary to stabilize the capitalist economic system and the capitalist social order (Jo 2009; Henry 2009b).

3.2 Industry and Finance

From a heterodox microfoundation perspective which links micro and macro, it is also apparent that industrial and financial sides of the economy are organically connected through the business enterprise. In terms of investment determination mechanism delineated above, investment is the source of reproduction of the enterprise as well as of the economy as a whole. The financialization of the capitalist economy (coupled with the concentration of industry and the decrease in capacity utilization ratio or the investment rate[8]) has increased the instability of the system. That is, the industrial innovation with which Schumpeter was concerned was outstripped by the financial innovation. Or, in Veblen's terminology, industry (making goods) is dominated by business (making money) in the capitalist society. Such an evolution of capitalist system has destabilized the economic system, as Minsky's financial instability pertinently explicates.

As argued earlier, the financial instability is a part of the whole story. The disturbances in the capitalist social provisioning process lie in not only finance but also industry. For example, a disturbance in the social process of production due to an unexpected rise in material input prices may lead to the rise in product prices (assuming profit mark-ups remain constant) across industry since industries are connected through the use of intermediate capital goods. Earning capacity for the business enterprise declines and hence business confidence in expected cash flows wanes. Expansionary investment projects are not likely to be implemented and the use of external credit (e.g., captialization of assets and external financing) stops (Veblen 1904; Wolfson 1994). At the same time, it should be noticed that the "reduction of output deepens the crisis, but at the same time is a factor in overcoming it, since it leads to the liquidation of commodity stocks" (Kalecki 1990, 50).

[8]It can be added that the degree of monopoly increases as a business enterprise becomes dominating in the market. Market uncertainty is under control by the dominant business enterprises. As a result, effective demand declines, investment further falls, and economic system increasingly unstable.

A story of business fluctuations focusing on business activities has important implications. First, business cycles are normal state of affairs in accordance with the evolution of capitalism. Second, since the cause of business fluctuations is associated with normal business activities which reflect social relations between classes, the evolution of capitalist institutions as an embodiment of social relations should be considered in the theory of business cycles. Thirdly, the overcoming of economic crisis or the stabilization of the capitalist economy should be found in the social relations. That is to say, it is *theoretically* possible to achieve full employment and the desirable growth rate of the economy by 'socializing investment' (Keynes 1936, 378), by government deficit spending (Kalecki 1943; Eichner 1976), or by industrial innovations (Schumpeter 1927; 1928; Kalecki 1990; Eichner 1976). However these measures depend *practically* upon the social relations, the political position taken by the state, the dominant ideology of the epoch, and the power and position taken by the working class (Kalecki 1990; 1943). In this respect, for example, public jobs created by the state or increasing money wage rates may reduce the instability of the system, but it does not necessarily remove the instability since the social provisioning process is controlled by profit-oriented business enterprises and the business-depenent capitalist state.

4 Conclusion

Heterodox theories of business cycles keenly explain that the instability of the capitalist economic system lies in the nature of capitalism. In particular, Schumpeter's instability thesis and Minsky's financial instability hypothesis relate business enterprises and business cycles. However, it is argued that these two prominent macroeconomic theories missing essential elements—class relations and social conflicts. So they are unable to see the instabilities of the capitalist order.

By looking closely at the business enterprises' decision making process in the context of monetary production economy, I argued that 1) business cycles are associated with normal business activities which reflect social relations between classes, 2) the evolution of capitalist institutions as an embodiment of social relations should be considered in the theory of business cycles, and 3) the overcoming of economic crisis or the stabilization of the capitalist economy should be found in the social relations. Therefore, heterodox economists should not constrain themselves into the instability of the economic system, if they are to provide deeper and extensive analyses of capitalism.

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