Preface

Despite an explosion of publishing activity since the Second World War, economic theory remains in a sorry state. The principal indictment against it is the failure of mainstream theory to provide convincing explanations of many economic phenomena, and to generate policy prescriptions which manifestly can solve outstanding economic problems.

Consider, for example, the theoretical explanation of the relative decline of the British economy. There is little consensus on this issue and many accounts are simply unconvincing. One of the most prominent explanations at present is that the level of wage settlements has exceeded the rate of growth of productivity, leading to excessive costs and a poor competitive position in the world economy.

However, this theory has to be buttressed with further explanations as to why supposedly rational workers would disregard their own long-term interests in a healthy economy and keep their wages 'too high'. Is this in turn due the 'coercive' unions, or to 'rigidities' in the labour market, or 'high' unemployment benefit? Notably, these additional explanations are either unsubstantiated or, if they are, the phenomena involved are often not peculiar to Britain. Thus these auxiliary hypotheses remain controversial and generally unconvincing as part of an explanation of Britain's relative decline.

Orthodox theory is equally at a loss to give a convincing explanation of the remarkable dynamism of the West German or Japanese economies, or the stagnation of productivity growth after reaching a high absolute level in the USA. Notably, all these countries have higher average wage levels than Britain, and this again questions the common presumption that wages are at the root of the problem. As to alternative explanations within orthodoxy the picture is discouraging. For instance, the coeditors of the influential *Brookings Papers in Economic Activity*, when addressing the issue of the stagnation in US productivity growth, concluded: 'Despite numerous studies of the slowdown its causes have remained largely a mystery. In the most comprehensive study to date, Edward Denison examined 17 alternative hypotheses and concluded that alone or in combination they could explain no more than a fraction of the slowdown' (Brainard and Perry, 1981, p. vii). This negligible success in explaining a basic problem, in the common postwar heartland of both world capitalism and economic orthodoxy, is a sad reflection on the subject as a whole.

Incidentally, when faced with theoretical problems such as this, orthodoxy immediately looks at explanations on the market side of the problem, concerning wages and costs, and often ignores the organization of production and the skills and practices of work. If, however, we take a different view then it can be seen that if the organization of production was improved to lead to higher productivity then higher output and higher wages could be compatible. On this basis it could be argued that there is a positive rather than a negative correlation between wages and output. In contrast, orthodoxy persists in its one-sided view and assumes that the firm is a black box which responds directly to changes in costs and the pressures of the market. Orthodoxy is not only unconvincing, it is blinkered as well.[1]

Inspecting the academic journals we are confronted with a great volume of complex formal theorizing and econometric technique. Yet the policies that economists have managed to derive from their theoretical armoury are typically simplistic and dominated above all by the political ideology that has been prevalent in the past. Either wittingly or unwittingly, this is adopted by most economists at the outset. Despite the high degree of formal sophistication, the ideological cart is often still in front of the theoretical horse.

For example, in the debates over public *versus* private ownership and planning *versus* markets, the economic theory usually serves as little more than a thin packaging for a very conventional ideological position of the Left, Centre or Right. The theoretical packaging serves largely to provide a covering of legitimacy, and as an enticement for the influential consumer of the economic advice. Politicians in or out of power are thus able to reinforce their prejudices and cloak them in some academic garb.

Economists can never free themselves entirely from ideology, nor indeed is it desirable that they should attempt to do so. But it is not a satisfactory states of affairs where science is dragged along by the political fashion of the moment; and it is even less acceptable when the ideologies are so crude and well worn. Many such ideologies have already been criticized with destructive effect on their central ideas, but these criticisms are happily ignored by many within the profession.

Alongside the crudely ideological employment of economic theory there is a continuing tendency to devote insufficient academic resources to the development of new solutions to obvious economic problems, despite the failure of the preceding economic policies to succeed. Thus, for example, unemployment is still alarmingly high in many Western countries, poverty still remains significant even in advanced industrial nations such as Britain and the US and relentless blows of famine strike the underdeveloped world. Yet these problems are not the main preoccupations of the majority of economists.

In contrast, mainstream economic theory often serves mainly as an aesthetic game for the theorist, with the prize of academic advancement for those who become adept in developing its skills and who can produce articles for the journals in their frequently stultifying format and style. A piece of work has a greater chance of publication and of becoming 'reputable' if it is infused with mathematical formalism and obscurantist terminology than if it directly and openly addresses the urgent problems of the day.

As an example, consider the following unwitting self-condemnation from Paul Samuelson (1962, p. 1), Nobel Prizewinner in economics and undoubtedly one of the foremost theorists of the postwar period:

> My own scholarship has covered . . . questions like welfare economics and factor–price equalization; turnpike theorems and osculating envelopes; non-substitutability relations in Minkowski–Ricardo–Leontief–Metzler matrices of the Mosak–Hicks type; or balanced budget multipliers under conditions of balanced uncertainty in locally impacted topological spaces and molar equivalences.

This, it appears, is the apogee of formalism for economic science. At the lower levels, students are initiated into this formalism in progressive but somewhat repetitive stages. The whole process has the aura of a protracted initiation ceremony, where future priests overcome their inclination to get involved in the grubby complexities of the outside world. As Neil Kay (1984, p. 188) puts it: 'the individual intent on pursuing a career as economist has to be bright enough to understand the abstract ramifications of neoclassical theory and dumb enough to have faith in them.'

Whilst some have been content with the theoretical ivory tower, others have been all too keen to use their economic theory as a weapon in an ideological crusade. For instance, with the ascendancy of the New Right in 1970s and 1980s, economic theory, even or especially of the most abstract kind, has frequently been employed as an academic legitimization for cuts in public expenditure and for an extension of private ownership and market competition.

It is a savage irony of our times that research into theoretical economics has become one of the many victims of this rightist creed. These ideas would not as easily have become implanted in high public places if they had not been backed by the 'pure theory' of researching economists: those from Adam Smith to Milton Friedman who have proposed a widespread extension of market relations and private enterprise, and urged a minimization of public funding upon which research is partially dependent. New Right thinking has been furthered considerably by the work of many others in publicly funded academic institutions. It has thus begun to saw off the very bough upon which it sits. In this manner, it could be said, such ideas represent a kind of professional suicide.

This is especially the case with the rational expectations hypothesis where it is actually assumed that everyone is basically aware of the underlying economic model. By implication, according to this theory, the economist has little else to offer because everyone is assumed to know in outline how the economy works. Yet economists have been all too eager to rush over this particular cliff, and a few uncritical and esoteric publications on the rational expectations model are currently the best ticket for promotion to an economics chair. Of course, every economist has a right to his or her beliefs (especially if these coincide with the chosen line of research) but there is no such right to carry millions of non-economists into the mire of poverty and destitution as a consequence of ideas which are formally 'interesting' but practically disastrous when applied to policy. The state of economic theory today would be farcical if it were not so tragic.

This state of affairs will not change quickly or easily, nor by the further scribblings of economic theorists alone. But nevertheless there is a duty for all economists to survey the imperfect state of their discipline, stand back for a while from the academic game, and address some of the core theoretical problems which are normally, and conveniently, ignored.

Answers to these problems are not easy to find, and this book does not claim to provide them. It is, however, an attempt to examine the fundamental assumptions of economic theory with a view to making a contribution to the construction of an alternative. A central argument is that conventional theory is guided by an outdated and theoretically unacceptable view of the individual which has been inherited from the classic liberalism of the nineteenth century.

A major theme of this book is the influence of institutions, social practices and history on our ideas, perceptions and actions. It would be inconsistent, therefore, to suggest that this or any other work is entirely original. It is necessary to acknowledge the effect of those very social and cultural forces in the process of its creation.

The reader will be able to trace the influence of several schools of economic thought on the present work. The first is the Post–Keynesian, including such figures as Joan Robinson and George Shackle, and particularly the works of John Maynard Keynes himself. The second is the Institutionalist School, overshadowed by Thorstein Veblen but including other more neglected figures such as Karl Polanyi. The third is the work of Marx, who, despite the efforts of Joan Robinson and others, is still vastly underrated as an economist.

There are also additional important influences, such as the Behaviouralist School, led by Herbert Simon, and an assortment of maverick figures, such as Frank Knight and Joseph Schumpeter. Whilst differences with the theory and policy standpoints of these economists remain, their effect on the ideas presented here should not be denied. This book is unashamedly eclectic in its attempt to incorporate valuable ideas that have been offered by other theorists, including both criticisms of neoclassical theory and elements of a constructive alternative.

There is a second reason why it would be a mistake to judge the present work on the grounds of originality. Whilst its central arguments are a marked departure from orthodoxy in economic theory, it draws on a variety of theoretical traditions elsewhere, namely within sociology, political science, anthropology, psychology and philosophy. On several key points there amounts to a consensus or near-consensus within these alternative disciplines, and notably this is often markedly dissonant from mainstream economic theory.

For example, apart from a few exceptions, the international consensus view within sociology, anthropology, political science and psychology seems to be that agents are not 'rational' in the way that neoclassical economists presume. The orthodox 'economic' canons of rationality are thus widely rejected elsewhere.

A great number of economists, however, remain cheerfully blinkered about their subject. The compartmentalization of the social sciences is reinforced by an attitude where economists can claim that they can have disregard for the contributions of other social sciences to the understanding of economic phenomena. An interview with Robert Hall of the Hoover Institute in the *Wall Street Journal* captured this insular outlook with the observation that the interviewee 'reflects the attitudes of his colleagues in saying he stops reading whenever he sees the word "sociological" in an economics paper'.[2]

One thrust of the argument in the book is not to claim a 'new' refutation of the assumptions of orthodox economics, but to show the poverty of its theoretical presumptions when compared with relevant work elsewhere. This gambit is not as simple as it may seem at first sight, partly because it is impossible to survey the entire field of social science, and partly because there is still fierce controversy within these other disciplines, despite the consensus on other important points.

It should not be suggested, however, that what is involved here is an assault upon or rejection of economics *per se*. The object of the attack is the prevailing orthodoxy, not economics as such. There is a prominent tendency within the economics profession to regard unorthodox approaches or schools of thought as beyond the realm of economics itself. This anti-pluralism or, more strongly, intellectual fascism, is not worthy of a subject which, for good or ill, claims great 'liberal' connections. Another aim of this work is to draw upon a wide range of literature in an attempt to establish the legitimacy of an alternative approach.

The precise definition and demarcation of the territory known as 'neoclassical economics' is, of course, problematic. Nevertheless, at the core of the body of theory usually titled thus is a set of ideas concerning rationality, knowledge, the economic process and the human agent.[3] Neoclassical theory involves:

1 rational, maximizing behaviour by all economic agents, whereby they are assumed to optimize according to preferences which are exogenously given;
2 the absence of chronic information problems, including radical uncertainty concerning the future, widespread ignorance of the structures and parameters in a complex world, and divergences in individual cognitions of common phenomena; and
3 a theoretical focus on movements towards or attained equilibrium states of rest, rather than on the continuous processes of transformation through historical time.

Within many of the top-ranking economics journals there has been an increasing flow of criticisms of neoclassical theory in the last 20 years. However, given the protocols of publication in these journals, these criticisms are often narrow in scope and formalistic in manner. Whilst many versions of neoclassical theory might prove vulnerable to a great number of criticisms of this type, it becomes necessary to provide a more comprehensive theoretical and conceptual framework if an alternative is eventually to be built.

This present work is a contribution to the project of developing economics along radically different lines. It cannot claim to provide a complete alternative. Given the task at hand this is unlikely to be accomplished by a single author, and even less likely in a single work. This book should be regarded as a signpost for a direction worth taking, not as a complete route map to, nor a survey of, the promised land.

Whilst neoclassical theory has come under increasing attack, it has in response widened and deepened its compass, to span a number of new issues, and in some respects its character has changed. Many of the past attacks on neoclassical theory purported to be devastatingly destructive, but the upshot was that orthodoxy adapted only slightly and went on much as before. These events should suggest that the defects of the neoclassical paradigm are more fundamental than many of the former critiques seemed to imply.

For instance, Piero Sraffa's (1960) work and the capital theory debates of the 1960s were successful in uncovering fatal logical inconsistencies in the neoclassical aggregate production function.[4] However, orthodoxy has either ignored these problems or shifted its emphasis onto the disaggregated versions of the theory. The remarkable survival of neoclassical theory after this destructive attack suggests that its 'hard-core' ideas were to be found elsewhere. They were not in its heroic acts of aggregation.

One outstanding theoretical issue is, therefore, to examine critically the deepest foundations of neoclassical orthodoxy. Notably, however, with a few important exceptions, these fundamental issues have not yet been addressed with sufficient attention by rival schools of thought. Indeed, there has been an understandable, but ultimately self-defeating, tendency by critics of orthodoxy to develop alternative formal models which differ from mainstream constructions in some (important) respects but still share the same core assumptions.

In this manner Keynes' economics were devalued, and their radical break from orthodoxy obscured, by the 'Keynesian' tradition of formalistic modelling in the two decades after the Second World War. It was the minority voices of Joan Robinson, Paul Davidson and a few others who kept the radical message of Keynes alive.

More recently, extensive formalistic developments have taken place within Marxism, using game theory and other mathematical tools.[5] This literature is not without value. Indeed, its analytical rigour is refreshing when compared with the scriptural dogmatism of the Marxian fundamentalists. But it incorporates core assumptions concerning rationality, knowledge and equilibrium which are essentially indistinguishable from neoclassical orthodoxy. Remove the dressing of radical language and we are presented with yet another version of mainstream theory, with its rationalistic and individualistic bias and its mechanistic model of the economic process. Contrary to many of my colleagues, I do not regard this development as wholly positive, nor one which can rescue Marxism from its own theoretical difficulties. On the contrary it is a sign of the decay of its inner core after its brief but much wasted heyday in the 1960s and 1970s. In particular, it is another formalistic diversion from the formidable practical problems of the real world, and a retreat into a scholasticism which seems to be sterile in policy terms.

In part it was disenchantment with the developments outlined above, in both neoclassical economics and some formalistic versions of 'Keynesian' and 'Marxian' theory, that led me to write the present study. After spending much of my academic youth on the diversionary delights of Post-Sraffian value theory, I became persuaded that time was too precious to be thus occupied for an entire career.

A central question, ignored by radical value theorists and many other critics of orthodoxy, is the nature of the human agent and the scope for rationality. Clearly, several versions of 'Keynesian' and 'Marxian' theory are happy to share orthodox axioms in this regard, and to perceive their differences with mainstream theory in terms of other assumptions, some of them quite superficial. But most crucially, the radical alternatives to neoclassical orthodoxy cannot continue to avoid the construction of an alternative theory of human agency, related to the economic context of social relation and institutions. If this work succeeds simply in establishing the urgency of this task then in my view it has not failed.

It would be too irksome to burden the reader with an account of how the present study relates to my own preceding work. It should simply be mentioned that research in the early stages of the production of this book led me to accept a more positive view of the value of psychology for economic analysis. Some lingering preconceptions that psychology was necessarily tied to an individualistic or crudely naturalistic outlook were removed. This change is partially a paradigm shift: not merely the discovery of unknown and valuable material. Indeed, there is a concern in the present work to relate the study of social and economic institutions to their natural and biological environment rather than to adopt the 'closed system' view of society or economy that is found in many versions in the social sciences.

This may contrast with my own preceding practice to some degree, but I shall leave it to the reader and critic to sort further through this dirty linen, if they are so inclined. My final word, before sentence is passed, is that as a theorist I would far rather be moving and developing roughly in the right direction, than being consistently and inflexibly wrong.

Bardon Mill, Northumberland