Economic Scholasticism and Capitalist Ideology

The intellectual achievements of the medieval scholastics consisted primarily of intricate and esoteric deductive elaborations of the religious first-principles which were nearly universally accepted without question. Within their static and rigidly fixed cosmology, the basis of their social and moral philosophy was the search for ways in which men could best understand the immutable laws of God's creation and bring their lives into complete harmony with these laws.

In the eighteenth century there was what superficially appears to be a major intellectual revolution. The cosmology implicit in Newtonian physics rapidly became the dominant intellectual framework for both the 'natural sciences' and the 'social sciences'. The Newtonian concept was basically that of an atomistic world governed by eternal and immutable mechanical laws of motion. All change was absolutely governed by these immutable laws. Change and movement could be understood as series of equilibria of atomistic elements, each self-contained and deterministically 'programmed' by the totality of forces buffeting it about in accordance with the laws of mechanics.

This point of view rapidly came to dominate social inquiry in the eighteenth century. The 'method of the new physical science became all important, for men proceeded to apply it in every field of investigation' (Randall, 1926, p. 261). The social sciences very rapidly came 'almost completely under the domination of the physio-mathematical method' (Randall, 1926, p. 261).

But the new world view was, in many essential respects, very similar to the older, medieval cosmology. A scholarly study of these similarities asserts that one can 'furnish an explanation of eighteenth-century thought, from a historical view, by showing that it was related to something that came before' (Becker, 1932, p. 29). This something was medieval cosmology. The eighteenth-century philosophers merely substituted nature and natural laws for God and God's laws.

> [The] disciples of the Newtonian philosophy had not ceased to worship. They had only given another form and a new name to the object of worship: having denatured God, they deified nature. They could therefore, without self-consciousness and with only a slight emendation in the sacred text, repeat the cry of the psalmist : 'I will lift up mine eyes to Nature from whence cometh my help' (Becker, 1932, p. 63).

David Hamilton (1970, pp. 19-20) has shown the result of Newtonianism in the social sciences:

> The eighteenth century viewed social forms as fixed in nature and what change took place was at most a quantitative one within fixed limits set by a natural order of things. The universe was a mechanical piece often likened to a clock whose moving parts, when once wound up by a divine Creator, would run eternally in the same pre-established mechanical arrangement. The best interest of man could be attained by an objective scrutiny of the workings of this mechanical universe. This inquiry was to be guided by reason, which would uncover the great principles by which the social universe was guided in its rhythmical pattern of movement. By laying bare these principles man would be able to conform to them and thus would enhance his contentment and happiness on earth. Misery and despair, the product of man's ignorance, which was also the source of his folly in flaunting these immutable natural principles, could be banished from the world.

Adam Smith's *The Wealth of Nations* was the denouement of the eighteenth-century philosophy. In place of Newton's law of gravitation Smith substituted 'self-interest'. A society which operated in accordance with natural law would be a private-property, capitalist, market system in which each atomistic individual exercised his 'natural right' to seek his own self-

interest. Each selfish, acquisitive individual would simultaneously promote the social good while he sought only his own welfare.

Smith's assertion that the 'invisible hand' of the capitalist, market system would harmonize all individual egoistic actions and lead to an 'optimal' allocation of productive resources has remained the most consistent basis for an ideological defence of capitalism down to the present time. 'The whole basis of modern price theory is to be found in Adam Smith without "modern refinement"' (Hamilton, 1970, p. 22).

Orthodox economists of the last 150 years, like the medieval scholastics, accepted the basic axioms of their system almost without question. They worked endlessly to create a brilliant deductive edifice on these axioms. By introducing complicated models of mathematical reasoning they have made it difficult, if not impossible, for all but the professional economist to follow the tortuous paths by which they arrive at their conclusions. Their conclusions are the same as Smith's: inherent in the capitalist economic system are forces which, if nurtured properly, will tend to create an ideal society.

The 'common core' or ideological and cosmological framework of economics has been only infrequently challenged. Rather, with scholastic zeal economists have endlessly produced esoteric trivia to embellish the decorative trim of their magnificent edifice. Milton Friedman (1970, p. 80) has succinctly described modern economics and modern economists:

> Economics is a scientific discipline that has a core that is common to almost all professional economists. *Naturally,* economists devote little professional research and writing — except in textbooks — to this common core. They concentrate on the issues that are on the frontier where economics is being made rather than taught or applied (italics added).

What is the common 'core' accepted by all and propagated in textbooks? How does it relate to the deductive esoteria at the `frontier' to which the modern scholastic economists are devoted?

Most college textbooks in microeconomic theory begin by describing an economic system in which: (a) market choices by consumers are determined by a coherent subjective preference ordering; (b) the decisions concerning what commodity mix to produce and how to produce it are governed solely by the desire of producers to maximize profits; and (c) buyers and sellers are pitted against each other in a market which is so large that no individual buyer or seller can, through his own purchases or sales, affect the market price.

Then, from certain axioms about the nature of consumer preference orderings and the technical relationships between inputs and outputs, a consistent line of deductive reasoning leads to the conclusion that an economic system of this description will allocate its resources in such a way that any possible change in production, distribution or consumption that could possibly make one person better off (leave him in a preferred position) could only be brought about by making someone else worse off (leave him in a less preferred position). In short, resources would be efficiently allocated so that, given existing tastes and the existing income distribution, it would be impossible to augment the aggregate value of production through a reallocation.

It is then argued that scientific objectivity prohibits the economist from making a normative choice between two situations which involve the bettering of one person or class of persons at the expense of another person or class of persons. Hence, the conclusion is reached that the criterion of 'economic efficiency' is scientific, whereas the criterion of 'equity' is not. The competitive capitalist economy is shown most perfectly to satisfy the criterion of 'economic efficiency'.1 Therefore, no other system can, on 'objective and scientific' grounds alone, be shown to represent an improvement over this capitalist price-market system. By extension, this doctrine becomes a claim that *laissez-faire* capitalism represents the best of all possible worlds.

To be sure, some flaws in the system are acknowledged. The principal admitted weaknesses are:

1. Some buyers and sellers *are* large enough to affect prices and, moreover, the economies of large-scale production seem to render this inevitable.
2. Some commodities are 'consumed socially' and their production and sale would never be profitable in a *laissez-faire* capitalist economy even though they may be deemed highly desirable by most citizens within the economy (e.g., roads, schools, armies, etc.).
3. The costs to the producer of a commodity may differ significantly from the social costs of producing that commodity, so that it is possible that for society as a whole the costs of production exceed the benefits of production for the commodity even though the producer still profits from making and selling it (e.g., the poisoning of the water and air by producers making profits but doing little or nothing about this evil side effect which could eventually endanger human life itself).
4. 4. An unrestrained price-market system appears to be inherently unstable and is subject to recurring depressions that incur enormous social costs.

The principal differences separating 'liberal' economists from 'conservative' economists stem from an inability to agree on the extent and significance of these flaws. It is generally agreed that to the degree that the flaws do exist and do disrupt the otherwise beneficial workings of the capitalist system, they can only be corrected by government intervention into the market system.

It is argued that government anti-trust actions can force firms to act *as if* they were competitive, and something called 'workable competition' can be achieved. Roads, schools, armies and other socially 'consumed' commodities can be provided by the government. Extensive systems of taxes and subsidies can be used to equate private and social costs where they differ. Finally, through the wise use of fiscal and monetary policy the government can eliminate the instability of the system.

The flaws are thus seen as minor and ephemeral. An enlightened government can correct them and free the 'invisible hand' once again to create the best of all possible worlds.

This, as I view it, represents a fair précis of orthodox economic ideology. I do not propose to argue here with either its assumptions or the reasoning by which the conclusions are reached. Rather, I wish to show how the rigorous working out of all the implications of this theory has led to a fruitless dead-end. One can argue that the ideology, when pushed to the logical extremes inherent in it, contains the seeds of its own intellectual destruction.

One of the most devastating intellectual attacks came from J. de V. Graaff's tightly reasoned book, *Theoretical Welfare Economics.* Graaff showed that economists had not really appreciated the long and restrictive list of assumptions necessary for the optimally efficient allocation of resources envisioned in the model of a competitive, free-market capitalism to be realized. He lists seventeen such assumptions which he has shown to be necessary (Graaff, 1957, pp. 142-54). Many of them are so restrictive that one must agree with Graaff that 'the measure of acceptance ... [this theory] has won among professional economists would be astonishing were not its pedigree so long and respectable' (Graaff, 1957, p. 142). A few of Graaff's seventeen conditions will suffice to illustrate the point. The theory requires (a) that any individual's welfare is identical with his preference ordering, i.e. that children, drug addicts, fiends, criminals and lunatics, as well as all other persons, always prefer that which is best for them; (b) that neither risk nor uncertainty is ever present; (c) that productivity is totally unaffected by the existing distribution of wealth; and (d) that all capital goods as well as consumer goods are infinitely divisible. These represent but four of Graaff's seventeen restrictive conditions which must obtain before the price-market system can achieve 'optimal economic efficiency'.

In the light of this, it is obvious that perfect competition could never be anything more than a normative model toward which government policies might attempt to move a capitalist economy. The goal could not possibly ever be achieved.

The next important piece of iconoclastic literature, well known to professional economists, is 'the general theory of the second best'.[2] In the words of the eminent economist, William J. Baumol (1965, p. 138):

> In brief, this theorem [of the second best] states, on the basis of a mathematical argument, that in a concrete situation characterized by *any* deviation from perfect' optimality, partial policy measures which eliminate only some of the departures from the optimal arrangement may well result in a net decrease in social welfare.

This important argument shows that, judged by the criterion furnished by the economic ideologists themselves, anti-trust actions or any other attempts by the government to bring about 'workable competition' may result in effects diametrically opposed to those envisioned by the authors of these policies.

Further work by Buchanan and Kafoglis (1963) and Baumol (1964) has shown that the rather naïve faith held by many economists that a system of taxes and subsidies could nullify the adverse effects encountered when private costs differ from social costs was based on an oversimplified view. Baumol showed that once again policies based on traditional arguments may actually diminish rather than augment social welfare (again using the orthodox economist's criterion of welfare).

In addition, concerning the stability of the system, Friedman (1953) and Baumol (1961) have shown that even if it were practically possible for monetary and fiscal authorities to use their powers in the manner prescribed in textbooks (and this is a big 'if') and if they were helped by a system of 'automatic stabilizers', the problem of instability would probably still be insuperable.

Finally, Arrow (1963) has shown that if we adopt consumer sovereignty as a fundamental normative criterion and simultaneously deny interpersonal comparisons of relative well-being (two of the basic tenets of orthodox economic ideology), then any coherent programme of government action must be imposed from above. No type of democratic voting under these two basic assumptions can be shown to yield a consistently ordered set of alternatives with which to guide government policies.

The significance of these recent developments in economic theory lies in the fact that each of these theoreticians has been in the mainstream of orthodox economics. Economic ideology as refined and systematized in the rarefied atmosphere of the professional academic economist has ended by destroying its own foundations.

Significantly, if one can judge by the best-selling textbooks in economics, at both the beginning and advanced undergraduate levels, a student who graduates from a North American or European university with a bachelor's degree in economics has probably never encountered these iconoclastic exercises which rigorously work out the full implications of orthodox economic theory.

1. Although Lange and Taylor (1964) have shown that an economy in which the means of production are collectively owned and for which the same assumptions are made will also result in a state of 'optimal economic efficiency'.

2. For a definitive formulation of this theory see Lipsey and Lancaster (1956-7).

References

Arrow, K. J. (1963), *Social Choice and Individual Values*, Wiley.

Baumol, W. J. (1961), 'Pitfalls in counter-cyclical policies: some tools and results', *Rev. Econ. Stat.*, vol. 43, pp. 21-6.

Baumol, W. J. (1964), 'External economies and second-order optimality conditions', *Amer. econ. Rev.*, vol. 54, pp. 358-72.

Baumol, W. J. (1965), 'Informed judgment, rigorous theory and public policy', *S. econ. J.*, vol. 32, pp. 137-45.

Becker, C. (1932), *The Heavenly City of Eighteenth Century Philosophers*, Yale University Press.

Buchanan, J. M., and Kafoglis, M. Z. (1963), 'A note on public goods supply', *Amer. econ. Rev.* vol. 53, pp. 403-14.

Friedman, M. (1953), 'The effects of a full employment policy on economic stability: a formal analysis', in *Essays in Positive Economics*, University of Chicago Press.

Friedman, M. (1970), 'On Paul Samuelson', *Newsweek*, 9 November, p. 80.

Graaff, J. de V. (1957), *Theoretical Welfare Economics*, Cambridge University Press.

Hamilton, D. (1970), *Evolutionary Economics*, University of New Mexico Press.

LANGE, O., and TAYLOR, F. M. (1964), *On the Economic Theory of Socialism*, McGraw-Hill.

Lipsey, R. G., and Lancaster, K. (1956-7), 'The general theory of second best', *Rev. econ. Stud.*, vol. 24, pp. 11-32.

Randall, J. H., Jr (1926), *The Making of the Modern Mind*, Houghton Mifflin.