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Growing Inequality in the Neo-liberal Heartland

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Introduction

Max Hastings, a former editor of the Daily Telegraph, is not known for holding strongly socialist views, but the extent of inequality in today's Britain has led him to write:

Today's filthy rich are wealthier, healthier and more secure than ever... It seems remarkable that any high roller these days resorts to fraud to enrich himself. It is possible to bank such huge sums legally that criminality seems redundant.¹

There is now a voluminous literature on growing inequality in Britain and the USA, not to mention an avalanche of newspaper articles on City bonuses and fat-cat salaries. For many years the conventional wisdom was that as countries grow richer, inequality at first rises but ultimately tends to fall when countries become 'fully industrialised', a hypothesis first advanced by Simon Kuznets in the 1950s. Over the past 30 years, however, inequality appears to have risen for the OECD countries taken together. This result is most strongly influenced by what has happened in the Anglo-Saxon world; notably, Britain and the United States where income and asset inequality today has returned to levels last seen in the 1930s. Squaring this trend with conventional economic theory has required telling a story about the growing premium placed on highly educated labour (including top entrepreneurial talent) in the 'new economy' pioneered in the Anglo-Saxon world while bemoaning the lack of dynamism of 'old Europe'. An alternative story traced below takes a closer look at the changing political and economic landscape of the period.

The rollback of the 'welfare state'---particularly in the UK, but also of its weaker US cousin set up under Roosevelt's New Deal---is the main legacy of the Reagan-Thatcher years, underwritten by subsequent governments in both countries and whose international expression is the Washington Consensus. The neo-liberal revolution of the 1980s had two critical implications for developmental alternatives to the pure free-market model; first, it was accompanied by the demise of the 'socialist' (USSR-style) centrally-planned economy option; secondly, in Europe it helped prompt the re-emergence of unfettered free-market capitalism as an alternative to the dominant post-war social democratic consensus.

Underlying the Reagan-Thatcher political project were structural changes in both the USA and the UK; notably, the decline of industrial capital and the trade unions, the rise of the international financial sector and the growing importance of the two-tier service economy; ie, low-wage and low-skill (eg, MacDonald's, Wal-Mart etc.) and high-tech (eg, Microsoft, Goldman Sachs etc.). The much-hyped 'new economy' has helped to fragment labour markets, change the structure of remuneration, weaken job security and the relative bargaining power of capital and labour and spread neo-liberal ideology. Growing inequality fed back into the political consolidation of neo-liberalism in a variety of ways ranging from the shift towards individual and corporate donations in the funding of political parties, the

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¹ Max Hastings 'They've never had it so good' *The Guardian*, August 6, 2005

concentration of media power in the hands of fewer owners and the reduction and commoditisation of politics into sound-bites and spin. In short, the modern Anglo-Saxon model has challenged the European 'welfare state' version of the market economy under which a relatively strong, democratically-financed state mediates conflicts between capital and labour and guarantees political and social cohesion and high levels of public provision.

It is crucial to emphasize that the Reagan-Thatcher project itself was a response to the decline of US and British industrial hegemony in the post-war period. Having been dominant globally for half a century, by the 1970s Britain was the 'sick man of Europe' and the US was rapidly losing its manufacturing dominance, in part because of an inflation-financed war, but crucially because it faced stiff competition from reconstructed Europe and emerging Asia---what today we would call a 'globalisation' effect. As profits fell² and share prices stagnated, Wall Street complained increasingly that the fault lay with stodgy corporate executives whose salaries were paid regardless of performance; the mantra of 'maximising shareholder value' began to be heard. Spurred on in the early 1980s by the appearance of corporate raiders and junk-bond finance, America's corporations began to restructure by selling off entire divisions, becoming 'lean and mean' and looking for new 'synergies' through mergers. Above all, 'maximising shareholder value' meant tying CEO remuneration to market performance, crucially through the use of share options, thus laying the basis for a quantum leap in executive rewards and the rise of a new class of super-rich whose influence soon spread to Britain.

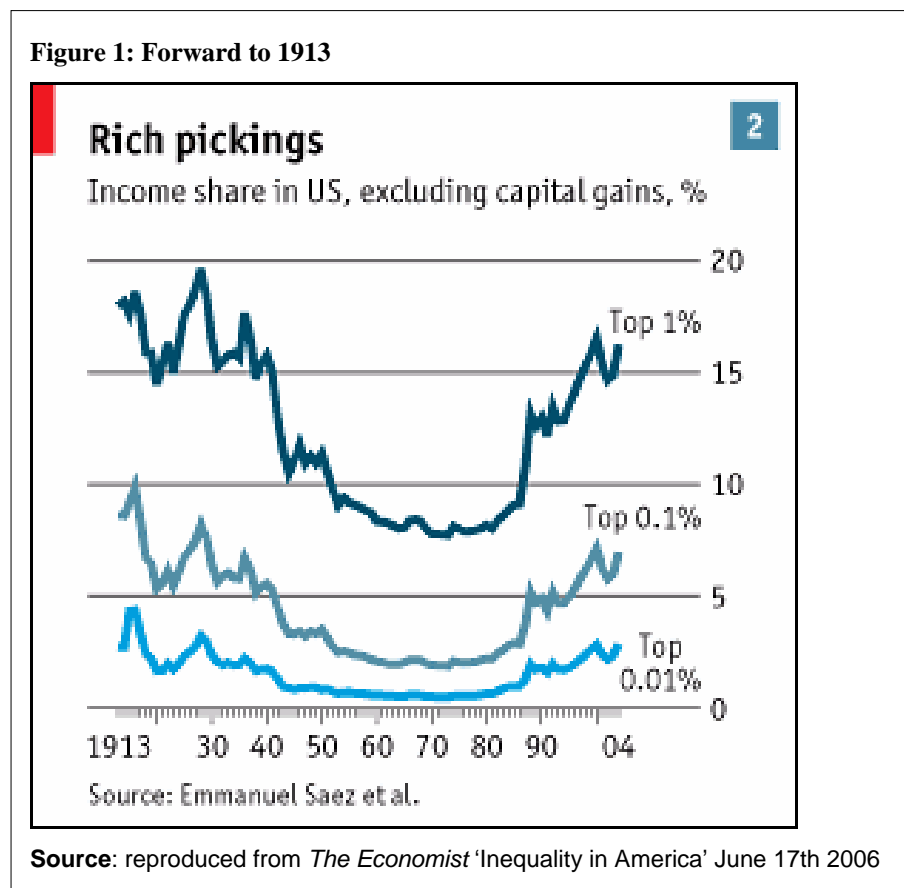
The Reagan-Thatcher period also saw the introduction of important legal milestones which would impact the distribution of wealth and power. In the UK, the explosive growth of financial services accelerated after the large-scale deregulation and streamlining of City transactions under the 'big bang' legislation of late 1986; this boost in comparative advantage gave London the decisive edge over Frankfurt and New York. The end of national wage bargaining and a variety of anti-union measures---symbolically capped by the defeat of the miners---constrained union activity; Britain's strong exchange-rate policy favoured the financial sector and helped underpin long-term deindustrialisation. Moreover, Britain's relatively lax tax residency law, coupled with the absence of the direct taxation of land or financial assets, lax inheritance laws and low rates of tax on income, has helped make the country a leading tax haven.

In the United States during the 1980s, airlines, trucking, banking and some utilities would be deregulated while industrial concentration---as reflected in growing corporate mergers---would grow explosively in the 1990s. As top corporations became more concentrated, CEO pay grew disproportionately, aided by favourable tax legislation. Reagan's Economic Recovery Act of 1981 greatly reduced top rate of personal tax while extending corporate tax write-offs and easing depreciation rules; further tax reductions followed in 1986. Income inequality grew strongly under Reagan and Bush I, a trend the Clinton years did little to reverse. Indeed, the 1997 'Taxpayer Relief Act' produced another bonanza for the wealthy: it is estimated for every \$1 in tax savings going to the bottom 80%, the top 1% of income earners saved over \$1000 in tax. While swathes of unionised skilled workers lost their jobs as traditional industries disappeared, the remuneration of top CEOs grew. As the president of the New York Federal Reserve Bank, William J McDonough, noted in a speech to mark the first anniversary of 9/11, in 1980 America's top executives on average earned about 40 times as

² See for example Glynn and Sutcliffe (1973) and Glynn (2005). An excellent recent discussion is Harvey (2005).

much as the average worker; by 2000 the ratio was 400:1, a jump impossible to explain by corporate performance.³

The Return of Inequality



The distribution of income in the US today is the least egalitarian of any of the major industrialised countries. This was not always true. The policies introduced under Roosevelt's New Deal in the 1930s improved the lot of the poor, the Second World War brought full employment and the post-war period saw further strides in reducing the extreme inequalities that characterised US capitalism in the early 20th century. However, over the past three decades the distribution of household income in the US has become as unequal as it was before the Great Depression.⁴ In broad-brush terms, this shift is explained by the fact that the rich---the very top percentiles of the household income distribution--- have become very much richer than before. By contrast, income has stagnated for the vast majority of Americans while the bottom twenty percent (the lowest quintile) is actually worse off than in 1970.

In the years 1970-2000, the pre-tax income share of the top 10 percent of households---the 9th or 'top' decile---rose from 23 to 44 percent. This is a startling figure. It means that the lion's share of the increase in US national income over the past 30 years has

³ See Pizzigati (2004: 451, 479). A study by Crystal concluded that differences in corporate performance explained only a tiny fraction of differences in corporate rewards; the main explanatory variable was corporate size; see K. Day 'Soldiers for Shareholders' *Washington Post*, August 27, 2000.

⁴ See Krugman (2004).

been captured by the top decile. Moreover, within the top decile, the inequality in income distribution is as striking as for the population as a whole. The 11-point gain in the share of national income going to the top decile has not been shared out equally. Far from it; the share of the lower half--from the 90th to the 95th percentile--has remained nearly flat, with the gain concentrated in the top 5%, and amongst these in the top 1%.⁵

US Census Bureau data confirm this trend and show that despite a GDP growth rate of 3.8% in 2004, only the top 5% of households experienced real income gains; incomes for the remaining 95% were flat or falling.⁶ Moreover, the combination of rising remuneration in the form of share-options, capital gains and other forms of asset appreciation, plus lax inheritance tax, means that America's wealth distribution looks increasingly like its income distribution. An unequal distribution of wealth helps propagate the transmission of income inequality from one generation to the next, thus re-enforcing the hierarchy of privilege.⁷ Krugman's warning is worth quoting:

The United States did not start as a society that you could describe as middle-class. We were a society with a dominant economic elite. We became a middle class society and thought we had reached a stable state. We were wrong because we have now moved right back to where we were before. We can no longer dismiss income distribution as a minor issue. In the United States it is now of the same order as economic growth in determining the standard of living of ordinary families. (Krugman, 2004; 79, 88)

Income Distribution, Technology and Taxation

The conventional economic explanation of why income distribution in the US (and to a lesser extent in the UK) has worsened is that the new economy puts a greater premium on high levels of education and entrepreneurship. Doubtless there is some truth in the 'skill-biased technological change' view, but recent studies confirm that the change in labour productivity patterns alone does not explain the very high degree of inequality now observed in the Anglo-Saxon countries.⁸ After all, the Nordic countries too enjoy high levels of productivity growth and have produced some of the world's most technologically advanced and dynamic industries, yet there is no sign that inequality has increased significantly in these countries over the past three decades.

Economists have traditionally seen economic growth and average productivity growth as two sides of the same coin. If labour productivity growth is high, one would expect the average real wage to be growing. In effect, labour productivity growth and wage growth in the Anglo-Saxon countries have become 'decoupled' from one another. An influential paper by Ian Dew-Becker and Robert Gordon (2005) of Northwestern University shows that in the USA over the period 1966-2001, only the top 10 percent of the income distribution enjoyed a growth rate of real wage and salary income equal to or above the average rate of economy-wide productivity growth. Median real wage and salary income barely grew at all. Half of the

⁵ In economist's terms, the upper tail of the income distribution conforms to a Pareto distribution. Thus, if (hypothetically) the richest, second richest and third richest person are A, B and C, if B were 10 times richer than C, we would expect A to be 100 (10x10) times richer than C. Some economists (eg, Martin Feldstein) regard this as a normal state of affairs and see no problem with the rich becoming richer as long as the poor are no worse off.

⁶ See 'Life in the bottom 80 Percent' *The New York Times*, September 1, 2005.

⁷ Following in Meade's footsteps, see Stiglitz (1969) for a model of the relation between patterns of inheritance and the distribution of assets and of income.

⁸ See for example Bernstein and Mishel (2007).

income gains in the US went to the top 10% of the income distribution, with little left over for the bottom 90%. Moreover, only half of the increase in inequality is attributable to gains of the 90th percentile relative to the rest. The other half is due to the increase in inequality within the top 10%.

Dew-Becker and Gordon (2005) argue that too little attention has been paid to the latter; ie, to the growth of inequality *within* the top decile. They attribute this growth in large measure to two complementary factors. One is the growth of 'winner-take-all' markets; markets in which enormous rents go to a few super-stars. The other is to the escalating earnings of corporate CEOs. Between 1966 and 2001, the median wage in the US has hardly increased in real terms. By contrast, average earnings of the top decile (the top 10%) increased by 58%. More striking still is the fact that over the same period real earnings of the top 1% increased by 121%; the corresponding figure for the top 0.1% is 256% and for the richest .01% is 617%. In their view:

Growing inequality is not just a matter of the rich having more capital income; the increasing skewness in wage and salary income is what drives our results This source of divergence at the top, combined with the role of de-unionization, immigration, and free trade in pushing down incomes at the bottom, have led to the wide divergence between the growth rates of productivity, average compensation, and median compensation.⁹

Three factors are of particular importance in explaining the explosive growth of CEO compensation since the early 1980s: share options, leveraged buyouts and the growth of financial corporations. Granting a low-priced option-to-buy shares (which can be exercised at some future date as the market rises) became a favoured way of rewarding top executives in the 1980s, initially because of their tax advantage.¹⁰ During the long boom of the 1980s-90s, as the use of share options became ubiquitous, CEO rewards grew hugely. In the words of *The Economist*: '...the story behind the growth of pay in the 1990s is really the story of the option. In 1992 S&P 500 companies issued options worth \$11 billion... in 2000 the number reached \$119 billion.'¹¹

The growth of super-rewards has often been a defensive response to the buyout-and-merger mania¹² on the past two decades. A leveraged management buyout is merely a debt-funded takeover in which a specialist company---aka, 'corporate raider'---gains control of the assets of a limited liability corporation, changes its status from public to private, uses its cash flow to service debt, sells off assets (typically greatly profiting the new owners) and ultimately sells the shell back to shareholders. Major swashbucklers in this business include Morgan-Stanley and Kohlberg-Kravis-Roberts, the firms behind the infamous RJR Nabisco buyout in the USA, and financiers such as James Goldsmith and Philip Green in the UK.¹³ Most important, in the USA, it is estimated that executives of non-financial companies represent only some 20% of the highest-paid CEOs (and even fewer in Britain). Riding on the back of the 1990s boom, financial consultants, senior investment bankers, fund-managers and other top people in the financial services sector have become prominent in the US rich-list. 'To qualify for Institutional

⁹ See Dew-Becker and Gordon (2005), abstract.

¹⁰ In the USA, options cashed in by executives become tax-deductible expenses for companies. By the 1990s, the use of options is thought to have cut billions off corporate tax bills (Pizzigati, 2004: 11).

¹¹ See *The Economist* 'A Special Report on Executive Pay' January 20th 2007.

¹² In 1999 alone, mergers in the US totalled \$1.75 trillion, ten times the value of mergers in 1990 (Pizzigati, 2004: 171).

¹³ For current concerns in the UK, see Will Hutton, 'Private Equity is casting a plutocratic shadow over British business', *The Guardian*, 23 Feb 2007; also see 'Special Report: Private Equity' *The Guardian* 24 Feb 2007.

Investor's Alpha magazine rankings of top hedge-fund managers in 2005, you had to earn \$130m [annually].'¹⁴

Equally, over the same period the incidence of total taxation in the US has become less progressive. A recent paper by Piketty and Saenz (2006) investigates this issue; the authors summarise their conclusions as follows:

The progressivity [*sic*] of the U.S. federal tax system at the top of the income distribution has declined dramatically since the 1960s. This dramatic drop in progressivity is due primarily to a drop in corporate taxes and in estate and gift taxes combined with a sharp change in the composition of top incomes away from capital income and toward labour income. The sharp drop in statutory top marginal individual income tax rates has contributed only moderately to the decline in tax progressivity.

During and immediately after the Second World War, the top marginal rate of income tax in the USA ranged from 84 to 94%. From the early 1950s to the mid-1960s, the top rate was 91 percent--levied on income in excess of \$400,000 (the equivalent of about \$2.64 million at 2006 prices). In 1971 under Nixon, the top marginal rate was reduced from 71 percent to 60 percent on taxable income in excess of \$996,000 (at today's prices), shortly thereafter it dropped to 50 percent and remained there until 1987. Under Reagan in 1988, it was reduced to 30 percent. 'These large reductions of the top marginal rate during the 1970s and 1980s were an open invitation to astonishing increases in executive compensation, and the invitation was widely accepted.'¹⁵

A recent study by Frydman and Saks at Harvard notes the remarkable stability of executive compensation from 1936 to 1969. During this 33-year period, the average 1.3 percent annual increases in executive pay were less than the wage gains made by the average American worker. By 1969, the inflation-adjusted value of executive pay had just barely returned to its pre-World War II level. Frydman and Saks also note that between 1969 and 1992, average total executive compensation increased by 75 percent, and that during the period 1993 to 2002 executive pay rose at an astounding rate of more than 14 percent per year so that at the end of the 20th century, "the real value of executive compensation was more than seven times its level prior to World War II."¹⁶

Although a similar trend can be observed in the UK, the same is not true for most other EU countries. In France, for example, whereas effective tax incidence thirty years ago was less progressive than in the United States, it is now more progressive. Indeed, the UK currently ranks 13th in the EU-15 income distribution tables. And although a nominally progressive government has been in power since 1997, a recent study by the Institute for Fiscal Studies shows that inequality has not improved since that date.¹⁷

The above picture also holds true for the distribution of assets, which strongly influences the distribution of earnings, and is in general even more unequal---and more difficult to measure because of inadequate data. The richest 10% of Americans own 70% of the country's wealth; the remaining 90% own what remains. More instructively, the asset

¹⁴ *loc. cit.*

¹⁵ See Michael H Trotter 'Tax plutocrats to restrain their pay' *Daily Report, Law.com*; Tuesday 27 February 2007.

¹⁶ Quoted in Trotter, *loc cit.*

¹⁷ See Brewer, Goodman et al (2006).

share of the bottom 50% of Americans is 2.5%. Much the same is true of Britain, although here a higher proportion on asset concentration is explained by land ownership.¹⁸

Inequality and Welfare

When discussing inequality, one must distinguish between income distribution before taxes and transfers (sometimes called the 'market' distribution) and income distribution after taxes and transfers. It is conventional when comparing countries to use the latter.¹⁹

That European countries are in general far more egalitarian than the United States is apparent from Figure 2 showing Gini coefficients measured on a comparable basis for the US and the EU-15.²⁰ Unsurprisingly, the most egalitarian countries (those with the lowest Gini values) are the Nordic group; at the other end of the table one finds the USA and the UK where inequality has grown significantly since 1980.²¹ The highest Gini values are those for Portugal and Greece, something hardly surprising given that these are the least developed members of the EU-15.

A slightly different way of measuring inequality is to compare the household income of different percentiles---1% slices---of the population. The greater the ratio of the 10th percentile (poor) ---those who occupy the 10th slice from the bottom--- to that of the 90th percentile (rich), the greater the degree of income inequality. Figure 3 shows these ratios for selected countries, and the ranking corresponds roughly to that found above where Gini coefficients are compared.

The most egalitarian countries are the Nordic group where the ratio in all cases is below 3.0. In the list of countries covered, Britain and the United States come close to last: the UK's ratio is 4.58 while that of the USA is 5.45. Mexico's score of 11.45 makes it highly unequal even amongst developing countries and is included for comparative purposes.

What is also important---but not illustrated here---is the dispersion of household income at the top of the distribution. Suppose we confined ourselves to the top 10% of the distribution---the top decile or 'the rich'---and sliced this into 10 levels from (relatively) less affluent to the very, very rich. Surprisingly, we would find that the degree of inequality amongst 'the rich' is no less than for the population as a whole. Indeed, it is at the top end of the distribution that inequality has been growing most quickly in the past 25 years. As one writer has put it, you are rich if you can live comfortably on the interest from your capital but you are very rich if you can live comfortably on the interest from the interest on your capital.

¹⁸ Recent sources are Cahill (2002); Lansley (2006); and Pearce (2004).

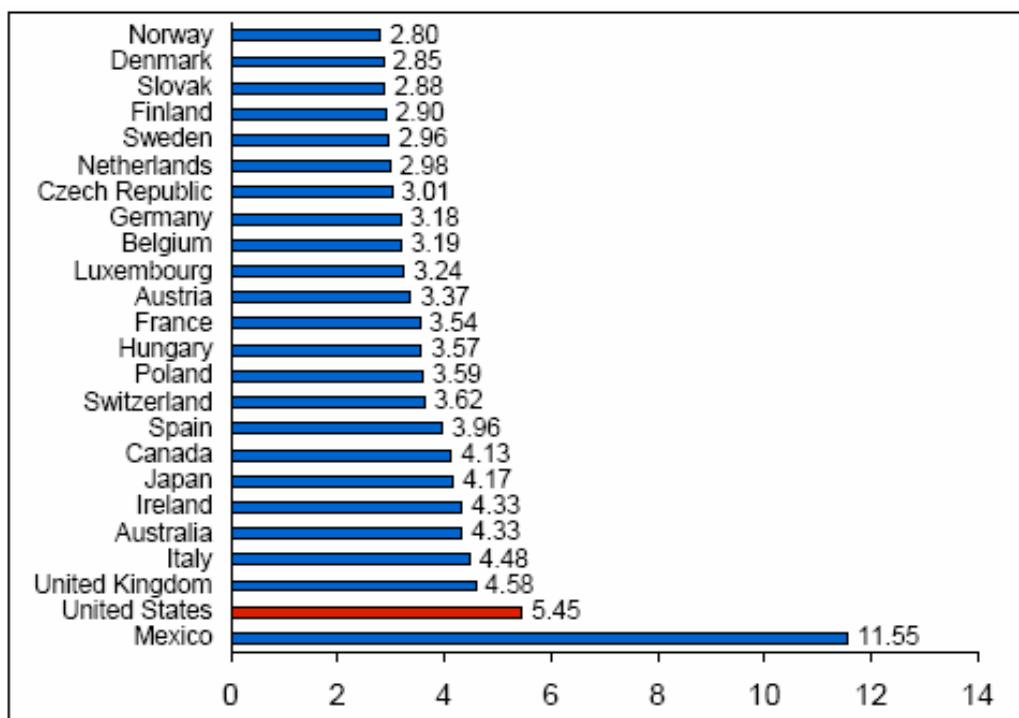
¹⁹ Equally, until recently, pre- and post-net transfer data was not available for the EU. This has been remedied with the development of the EUROMOD dataset, developed at Cambridge to estimate and compare the effects of taxes and transfers on personal and household income across the EU-15.

²⁰ The Gini calculations refer to the mid-1990s and are based on the Luxembourg Income Study (LIS) household data, 1979-99, the most recent attempt to measure income using a standardised definition. For details, see Smeeding (2002). Gini values for Portugal and Greece, excluded from the Smeeding study, are taken from Papatheodorou and Pavlopoulos (2003) whose data is from the Consortium of Household Panels for European socio-economic research (CHER);.

²¹ Although Smeeding (2002) uses several measures of income inequality besides the Gini coefficient, I have ignored them since they all give roughly the same country ranking.

| Figure 2: Gini Coefficients by Country (1990s) | |
|---|-------------|
| Sweden 1995 | .221 |
| Finland 1995 | .226 |
| Luxembourg 1994 | .235 |
| Netherlands 1994 | .253 |
| Belgium 1997 | .255 |
| Denmark 1997 | .257 |
| Germany 1994 | .261 |
| Austria 1995 | .277 |
| France 1994 | .288 |
| Spain 1990 | .303 |
| Ireland 1987 | .328 |
| Italy 1995 | .342 |
| UK 1995 | .344 |
| Greece (CHER, 1999) | .362 |
| Portugal | .375 |
| <i>EU-15 average</i> | <i>.288</i> |
| | |
| USA 1995 | .372 |
| Source: Smeeding (2002); Atkinson (2003). | |

Figure 3: Household Income Inequality for Selected Countries (ratio of 90th to 10th percentile)



Source: Smeeding (2004) in Schmitt and Zipperer (2006)

Growing inequality is at least in part a political phenomenon, attributable to the policies followed by specific right-wing governments rather than simply a deterministic attribute of globalisation.²² This point emerges clearly when looking at the UK under Thatcher in the 1980s. In the period 1984-90, the Gini coefficient for the UK rose by 10 points. This change was larger than that in any other OECD country, and it happened more quickly. Not only did inequality increase more rapidly in the UK than in the USA in this period, but there were differences in its root causes. In both countries the rich grew richer; in the UK however, a combination of de-industrialisation, a steep rise in unemployment and the political assault on trade-unions and welfare means that the poor grew poorer faster in Britain than in the USA.

The assault on welfare in the UK was not just a matter of bashing organised workers. Government statistics for the period 1980-2000 show the number of children in poverty to have risen from 1.4m to 4.4m and a doubling in the number of pensioners with less than half the average income.²³ By the turn of the century, not only was Britain less equal than other EU states at a comparable average income level, its social and economic infrastructure was in tatters. It is important to add that since 2000, some progress has been made in improving infrastructure and reducing poverty at the bottom of the income pyramid, although not in reversing inequality trends.²⁴

Luxury Fever

The American economist Robert Frank coined the term 'luxury fever' nearly a decade ago to describe the growth of consumerism in the United States since the early 1990s.²⁵ The reason we buy ever more elaborate consumer goods, Frank argues, cannot conceivably be because they do the job ever more efficiently. More elaborate goods may in some cases be more efficient, but rarely is this in proportion to the rise in their price tag. Rather, it is because as the income distribution becomes more skewed, the spending patterns of the super-rich are spreading to an ever wider public.²⁶

Whereas in the 1950s the average American middle class family might have been satisfied with a 3 bedroom house with a carport, by the 1990s only 4-5 bedrooms would do and a two-car garage was essential. The American generation of the 1990s may have owned more cars than their parents, but they did not have more children. Yet the average American house built at the end of the 1990s was nearly twice as large as its 1950s counterpart. The average American car of the same year costs 75% more than a decade earlier. Americans, whatever their social status, find it increasingly difficult to 'keep up with the Joneses', and this concerns everything from the sums spent on weddings to the price of a house in an area with a good school to the university fees which must be paid if the children are ever to find jobs at a salary commensurate with the life style which their parents have taught them to aspire.

Crucially, says Frank, there is a price to pay:

²² See Paul Krugman, 'For Richer' *New York Times Magazine*, Oct. 20, 2002

²³ See for example Gordon and Townsend (2000).

²⁴ See Toynbee and Walker (2005); also Paxton and Dixon (2004).

²⁵ See Frank, R H (1999).

²⁶ A recent academic study offering a fundamental critique of economists' treatment of consumption is Offer (2006).

All of us, rich and poor alike, but especially the rich---are spending more time at the office and taking shorter vacations; we are spending less time with our families and friends; and we have less time for sleep, exercise, travel, reading, and other activities that help maintain body and soul. Because of the decline in our savings rate ... a rising number of families feel apprehensive about their ability to maintain their living standards during retirement. At a time when our spending on luxury goods is growing four times as fast as overall spending, our .. public infrastructure [is] deteriorating. ... Poverty and drug abuse is on the rise ... A growing percentage of middle- and upper-income families seek refuge behind the walls of gated communities.²⁷

Frank's reference to growing insecurity is resonant with ILO-based work by Guy Standing on labour market insecurity.²⁸ But Frank makes greater use of the conventional economic notions of cost externalities and market failure. An individual's decision to buy this house or drive that car almost always has an effect on the rest of us, often negative and unintended. My decision to drive to work instead of taking public transport---bearing in mind the woeful state of public transport in the US and Britain---may result in a negligible addition to congestion or pollution, but if most of my neighbours decide to do so as well that day, the result is a situation for the collective which none of us could foresee. Similarly, I may decide quite sensibly to take out an extra mortgage to move up to a large detached house, but if everybody gets in on the act, house prices rise, there is greater pressure on urban infrastructure, less green area and so on. In short, what may be a sensible decision taken in isolation turns out to be a costly and unjustifiable from the point of view of the community. This 'paradox of isolation' is one of the fundamental characteristics of market-based choice. This is why markets often need to be regulated and collective decisions need to be made through representative political institutions rather than at individual level in the market.

In much the same vein, Judith Schor at Harvard²⁹ has written on why we increasingly want what we don't need. Schor's key point is that our reference groups are widening and that today, comparisons are made over a much broader range of goods and services. Two generations ago, the typical middle class family tended to view its consumption status in relation to that of the Jones's next door, or perhaps by looking slightly further afield at how the life style of the local doctor or bank manager. That appears to have changed: the revolution in the media, in advertising and the rise of celebrity culture means the same family now looks further up the income ladder.

Consumption status is conferred by a far wider range of goods and services; the phrase 'aspirational goods' (aka, lifestyle items) has entered common usage. It is no longer enough to have a detached house or a nice family car in an age where virtually everything you buy---including where you have your hair cut or take your holidays---is scrutinised. And it is not just adults who compare themselves to others; children are subject to intense peer pressure about what designer jeans they wear or whether they sport the coolest brand of trainers. As Schor notes, 'when the children of affluent suburban and impoverished inner city households both want the same Tommy Hilfiger logo emblazoned on their chests and top-of-the-line Swoosh on their feet, it's a disaster'.³⁰

²⁷ See Frank (1999: 5).

²⁸ See Standing (2004).

²⁹ See Schor, J (1998).

³⁰ See Schor (1998: 5).

The change in people’s aspirational goals is reflected in survey evidence which relates the level of household income considered ‘desirable’ to that actually enjoyed. Clearly, very poor households report that they need more money to live properly. What is surprising is that aspirations rise in proportion with income, so that even the rich feel they need more money to enjoy a truly comfortable lifestyle. The aspirational lifestyle is defined by the consumption pattern of those further up the income ladder. As the income ladder is extended ever further upward, so the pressure to earn and consume more increases. It is this fact above all, Schor argues, that helps explain the demand side of the debt-fuelled consumer boom in the USA and the UK to which we return shortly.³¹

Paying the bill: longer working hours and years

If the new consumerism is driven by the growing inequality in income distribution, so too consumerism drives inequality as top earners aspire to ever more luxurious lifestyles funded by spiralling annual earnings running into single and double digit millions. And as top earners pull in more, so too, those on the lower rungs of the ladder of riches demand more, skewing the income distribution even further. But growing inequality entails many other costs.

| Figure 4: Annual hours worked per full-time person in active labour force: 1883, 2000 | | |
|--|-------------|-------------|
| Total Employment | 1983 | 2000 |
| Netherlands | -- | 1371 |
| Norway | 1485 | 1380 |
| Germany | 1674* | 1463 |
| France | 1672 | 1500 |
| Denmark | -- | 1504 |
| Belgium | 1684 | 1530 |
| Switzerland | -- | 1568 |
| Italy | 1694 | 1619 |
| Sweden | 1520 | 1625 |
| Ireland | 1910 | 1690 |
| UK | 1713 | 1707 |
| Portugal | -- | 1708 |
| Finland | 1787 | 1727 |
| Spain | 1912 | 1814 |
| USA | 1824 | 1834 |
| * 1983 figure for West Germany source: OECD Employment Outlook, Annexe Table F., OECD 2003; ILO (1999) ‘Americans work longest hours among industrialized countries’ ILO News, Monday 6 September 1999 | | |

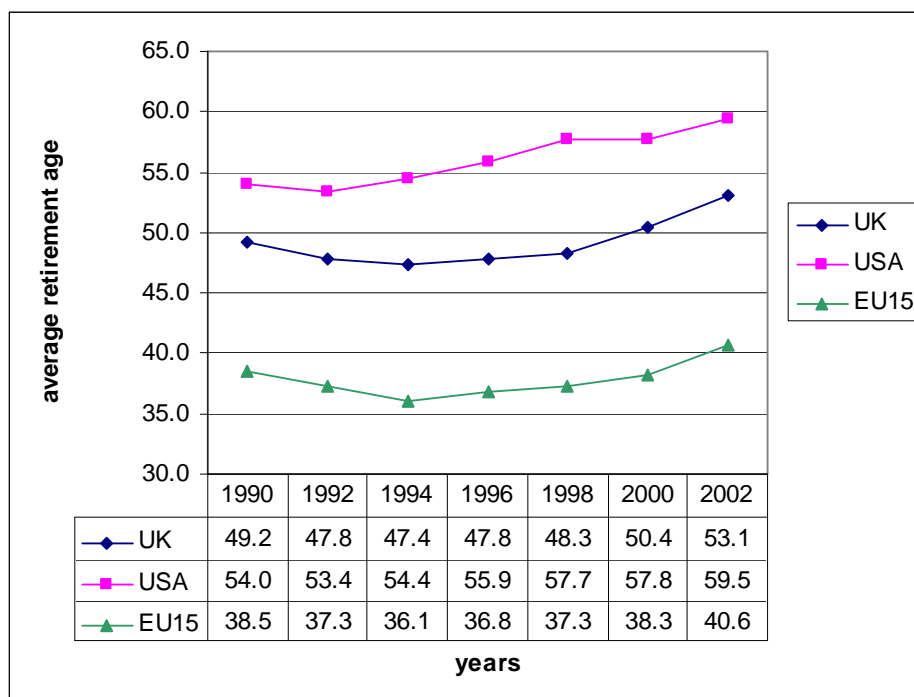
³¹ I am indebted to Jennifer Shaw of the University of Sussex for comments on the ‘drivers’ of consumerism; for the sake of brevity I have excluded important factors such as advertising, declining real prices of many goods and the influence of governments on ‘lifestyle items’; eg, the notion that the ‘range of choice’ of public goods should be market-driven, that super-casinos expand choice and so on.

These ‘other costs’ include working more hours, retiring later, saving less and becoming more indebted.³² More generally, the renewed rise in sumptuous private affluence is associated with greater neglect of economic and social infrastructure, declining social cohesion and a variety of social ills now being catalogued under the new label of ‘social epidemiology’.

To earn the money needed to meet their aspirations, American and British families are putting in longer working hours, and the single earner family is being replaced by one in which both partners have a job. This trend is borne out by a comparison of annual hours worked and female labour force participation rates. Americans, followed by Britons, work the longer annual hours, and women work more, than in other industrialised countries. In America, moreover, the proportion of workers remaining in the workforce after 60 and indeed well beyond retirement age is greater than in most European countries.

US workers put in the longest hours on the job in industrialized nations: 1834 hours per capita in 2000. Based on OECD and ILO data, the US pattern of increasing annual hours worked per person, which totalled 1,824 in 1983, contrasts most sharply with those of European workers, who are spending progressively fewer hours on the job, particularly in countries such as Norway and The Netherlands where hours worked in 2002 were, respectively 1371 and 1380 per year. In France, full-time workers put in 1500 hours in 2002 versus nearly 1700 in the 1980s. In Germany, average working hours for 2002 were 1463 versus 1674 in 1983. Workers in the United Kingdom, who put in 1707 hours annually in 2002, appear to have neither gained nor lost much free time since 1982 when they worked 1713 hours.

Figure 5: Selected retirement ages and employment rates for group 55-64, 1990-2002



source: *OECD Factbook 2006: Economic, Environmental and Social Statistics.*

³² The seminal work on the US is Schor (1992); note that this work has been questioned by various authors, including Bluestone, B and S Rose (1997). A recent critique is summarised in: *The Economist* ‘The Land of Leisure’ Feb. 2, 2006.

Not only do Americans work more per year, they appear to remain in employment longer. Figure 5 contrasts the trend over 1990-2002 in average employment rates for workers aged 55-64 in the USA, the UK and the EU-15. In 1990, 54% of American workers in this group were in full time employment compared to 49% in the UK and 39% for the EU as a whole.³³

While the trend is upward in all cases, today nearly 60% of older American workers are in full-time employment, considerably more than the proportions in the UK and the EU-15 as a whole. While this state of affairs might have worrying implications for pension provision in some EU countries, it does support the argument that Americans not only work longer hours but enjoy fewer years of retirement.

Paying the bill: Health Costs

A century ago, poverty was still defined in absolute terms and the poor died of malnutrition or were swept off by epidemic diseases. As Europe grew richer during the years of post-war reconstruction, better infrastructure, higher wages and new welfare provisions rescued most people from the threat of absolute deprivation. Writers on health and social policy speak of the 'epidemiological transition', meaning that as countries grow richer, the traditional 'diseases of the rich' such as stroke and heart disease reverse their social class incidence and become associated with the poor---a most striking example today being the incidence of obesity. And as absolute deprivation shrank, so poverty itself began to be redefined in relative terms.³⁴ Today, for example, the household 'poverty line' in most EU countries is typically defined as 60% of median household income.

It may appear paradoxical that looking at within-country and between-country data, there is a significant relationship between health (as measured by life expectancy) and per capita income in the former case but little relationship in the latter. Hence, although the income disparity between Bangladesh and the Harlem district of New York City is huge, infant mortality is higher in Harlem. The apparent paradox is resolved if we accept that what affects health is not absolute income, but income relative to others---a key marker of social status in society.

Layard's observation that growing prosperity is not accompanied by growing 'happiness' has become today's academic cliché.³⁵ There is now ample evidence that the growth in inequality---the rise of the super-rich and the celebration of new life styles about which New Labour has been so 'intensely relaxed'---is associated with poor health, high rates of violence and low levels of social capital. Wilkinson (2005) cites various studies showing the difference in life expectancy (measured from age 16) between rich whites and poor blacks in USA is about 16 years for both sexes. The studies quoted cover 23 different areas; in all cases, differences in area incomes are closely associated with differences in death rates. Wilkinson suggests that health inequalities related to different socioeconomic status may deprive the average poor person of 20-25% of the length of life enjoyed by the rich. He adds:

³³ It should be noted that the EU-15 average includes the UK; also, the average does not show the considerable variation between different EU countries in employment rates for the 55-64 age group.

³⁴ A pioneering book on the importance of *relative* poverty is Runciman (1966).

³⁵ See Layard (2005).

What would we think of a ruthless government that arbitrarily imprisoned all less well-off people for a number of years equal to the average shortening of life suffered by the less equal of our own societies? [Wilkinson (2005: 18)]

Nor is this phenomenon associated purely with poverty: the finding holds across all classes, while slope of gradient varies from one country to another and across time. It is greater in the US and Britain than in the Nordic countries. For the UK, in a well-known study of the civil service, Rose and Marmot (1981) took a large sample of male office employees and found that death rate from heart disease among low-status was four times as high as among highest ranks. Donkin, Goldblatt and Lynch (2002) report that whereas in early 1970s the difference in life expectancy between social class V (unskilled manual) and social class I (professional) was about 5 years, by early-mid 1990s difference was 9.5 years for men and 6.5 for women. As Wilkinson writes:

Inequality promotes [survival] strategies that are more self-interested, less affiliative, often highly anti-social, more stressful and likely to give rise to higher levels of violence, poorer community relations, and worse health. In contrast, the less unequal societies tend to be much more affiliative, less violent, more supportive and inclusive, and marked by better health more unequal societies tend to have higher rates of violent crime and homicide, and ... people living in them feel more hostility, are less likely to be involved in community life, and are much less likely to trust each other; in short, they have lower levels of social capital. [Wilkinson (2005: 24)]

In this context, Robert Putnam's well-known study *Bowling Alone* shows the decline of community bonds---what he calls 'social capital'---in the US after the 1950-60s, a period of growing inequality. Putnam's work reveals that in the more unequal parts of the US, where participation in community life is lower, it is particularly the poorer people who have ceased to participate. Where there is more income inequality, poorer people are more likely to feel out of place participating in community groups, more likely to feel ill at ease and to think that they will make fools of themselves and be looked down upon. Equally, there is a clear link between growing inequality and the rise of fundamentalist religious communities, which provide a replacement for traditional support networks.³⁶ The right-wing political implications of this trend in the United States have become manifest in recent years.

Paying the bill: falling household savings and growing debt

If the growth in inequality has helped fuel a consumer boom, this state of affairs has serious macroeconomic implications too---not just for the USA but for the rest of the world. The relatively favourable growth record in recent years of the USA---and to a lesser degree of Britain---compared to Europe is largely explained by a long consumer boom financed by growing household borrowing and, helped along in the US since 2001 by a ballooning budget deficit.³⁷

Although one hears much about the US 'twin' deficit, in reality it is a 'treble' deficit encompassing the household, government and external balances. Both the government and the private household sectors spend more than they save, and this gap is reflected in an

³⁶ In this context, see for example M Gladwell, Letter from Saddleback; the Cellular Church, *New Yorker Magazine*, September 11, 2005.

³⁷ Much of the current section is based on Irvin and Izurieta (2006).

external deficit on current account equivalent to nearly 7% of GDP that must be financed from abroad. At present, the US spends about 50 percent more than it earns in the world market. In absolute terms, the 2005 current account deficit was close to \$800bn, by far the largest deficit ever recorded. To get some idea of the magnitude of this sum, if we add the external deficits of the poorest third of the world's 168 countries, the resulting figure represents barely one-twentieth of the US deficit.

The US Government's budget deficit on its own would not be terribly worrying if were it not for a further factor: US households now spend more than they earn to a degree that offsets net corporate savings. Whereas, historically, the household sector was a net lender to the tune of about 2.5% of national income, today households have become net borrowers of about 6 per cent of national income.³⁸ Clearly, any fall in household borrowing would cause the economy to contract unless offset by more spending elsewhere; eg, by Government. If financial markets worry when there is an external deficit, they worry even more when there are government and private deficits as well.

Since the US private and government sectors have ceased saving, it is foreigners who must save---chiefly by lending their savings to the US. As foreigners use their surplus dollars to purchase US assets, the US has moved from being a net creditor to a net debtor to the tune of roughly \$4trn. Overseas investment in the US at the end of 2005 reached \$14trn, about the same as the country's national income. Servicing US net indebtedness has begun to add to the country's current deficit.

Most important, the deficit has increased despite an effective dollar devaluation of 17 percent over the three-year period 2002-04. If adjustment is sought by recourse to devaluation alone, then it is clear that much larger effective devaluation is needed. But a very large devaluation would most likely be accompanied by a US---and thus a world---recession. Such a recession would hardly provide a climate conducive to US export growth. In sum, the US deficit is huge, it is growing and a precipitous cure brought about by markets alone might prove very costly. Once financial markets believe that the US deficit is truly unsustainable, the prophecy will become self-fulfilling.

Why US growth cannot be sustained

The spiralling growth in US and UK household debt is closely related to the liberalisation and growth of the financial market. The stock-market boom of the 1990s morphed into the real-estate boom of the current decade, with low interest rates, rising asset prices, mortgage withdrawal and unsecured credit card debt helping to fuel faster growth in private spending than of household income. For a variety of reasons, the growth in US household spending in the past decade has been relatively painless. Holding gains have been turned into ready cash because of the ease of re-mortgaging, and low interest rates have kept financial markets well-lubricated. But there are at least three reasons why this pattern cannot persist unchecked.

First, any slowdown in asset appreciation tends to generate uncertainty about the sustainability of future gains, and hence lead to a further slowdown. Secondly, although the value of asset growth may slow or even reverse, consumer liabilities remain the same. Under

³⁸ In 2005, unsecured credit-card debt alone in the US amounted to \$750bn; in the UK, total household debt now amounts to over £1 trillion, the highest per capita in the EU.

conditions of very low inflation, the value of household debt erodes only slowly. Thirdly, although a slowdown in private spending can be offset by an increase in government spending, the scope for such counter-cyclical policy has been reduced by the Bush administration. When the stock-market bubble burst in 2001, Washington responded by lowering interest rates and granting swingeing tax cuts for the rich. While Washington's monetary stance has since tightened, tax cuts cannot easily be clawed back, so narrowing the scope for Government to prime the pump in future. The budget deficit is well in excess of the 3% limit that orthodox economists deem it prudent for a country to observe while the net liability position is about 50% of GDP. In short, if the private household sector cuts its own spending and returns to a sustainable savings path, government must run ever growing deficits to sustain aggregate demand at a time when the scope for so doing has greatly diminished.

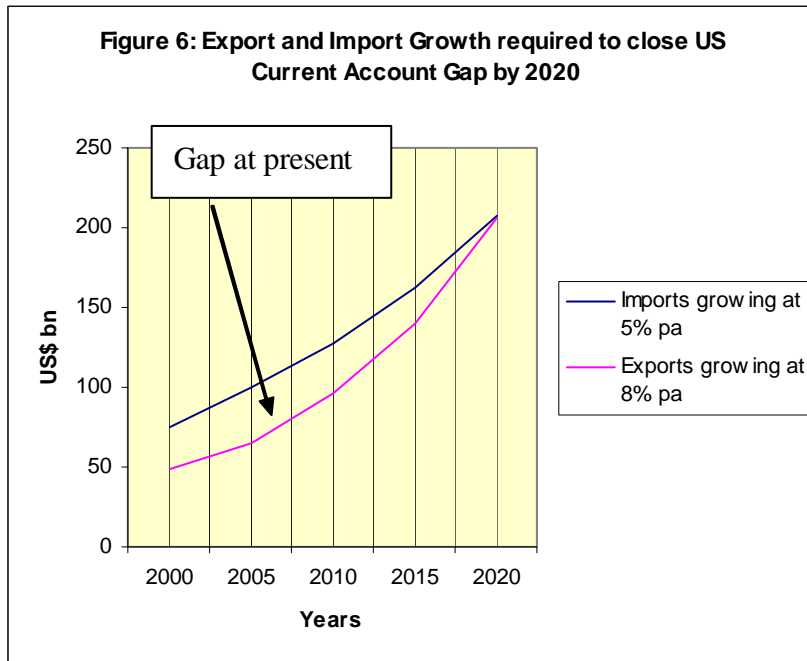
The UK position bears striking similarities to that in the US. UK net household debt is large and growing, and the UK's external current account deficit is the largest of the EU15 states. At the same time, the UK is a much smaller economy than that of the US, and its external deficit is largely with the rest of the EU (bearing in mind that the EU as a whole runs a current surplus). Equally, the UK Government deficit represents a smaller share of GDP, as does the public borrowing requirement. Since the UK does not belong to the eurozone, it has little say in shaping an EU response to the US deflationary danger. Nor does the UK Treasury appear very concerned about this danger judging by the Chancellor's silence on these matters.

The response of the Bush administration to growing external debt has been confused and confusing. The US Treasury appears to believe in a 'strong dollar' solution sustained by increases in productivity resulting from a synergy between the foreign capital keen to invest in the US and the resilience of 'corporate America'. The Federal Reserve appears keener on market-led exchange rate adjustment combined with action to reduce the 'world savings glut'.³⁹ This response mirrors the IMF view which, succinctly stated, is that a full-employment growth path is sustainable as long as governments practice fiscal and monetary restraint and prices---chiefly the prices of foreign exchange and labour---are allowed to adjust freely (including free appreciation in surplus countries). While the precise degree of dollar devaluation required is not stated, the unofficial view in Washington is that a real dollar devaluation of 15-20% would suffice to restore overall trade balance as long as the rest of the world allows similar adjustment. Since late 2006, the markets have forced the dollar down nominally by nearly 30%. Let us assume that this leads to a 15% real devaluation. While it is true that the response-lag may be as much as 2-3 years, whether a real devaluation can work depends to a significant degree on whether financial sentiment anticipates this lag correctly.

Why is nominal exchange rate adjustment unlikely to restore balance? First, a large nominal change may bring about only a small real change. A number of US trading partners (eg, China, Malaysia, Hong-Kong) have effectively pegged their currencies to the dollar and are unlikely to be persuaded to accept the slowdown in export-led growth that a major currency revaluation would entail. Secondly, a real fall in the dollar will not lead automatically to an external account improvement. This is due in part to the fact that dollar depreciation has a 'wealth effect'. When the real value of the dollar falls, US holders of (say) euro-denominated assets gain and consequently feel richer and continue spending. Finally, the trade gap is simply too large. Exports would need to grow 3% faster than imports for fifteen years merely

³⁹ See for example Ben S Bernanke 'The Global Saving Glut and the U.S. Current Account Deficit', Sandridge Lecture, Richmond VA, March 10, 2005.

to bring US exports and imports to balance (see Figure 6). Such a turn-around could not be engineered by price-adjustment alone but would require constraining import growth via a major slowdown in economic activity. But a recession-induced adjustment would be painful not just for the US, but would threaten the international economy as a whole. Exchange rate adjustment may be desirable, but it needs to be accompanied by increased absorption in the rest of the world. Since US imports are growing steadily at about US\$ 200 billion per year and exports at about US\$ 100bn, a *full* correction of the current account which avoids US recession requires the rest of the world to absorb about US\$ 850bn of exports (\$750+\$200-\$100 billion) next year and even more in future years.⁴⁰



source: Irvin & Izurieta (2006)

The US trade gap cannot be closed without significant world economic acceleration. The main surplus countries are Germany and Japan who together absorb over 40% of the US deficit, with Russia, Saudi Arabia and China together accounting for a further one-third. Russia and Saudi Arabia are large energy exporters, and their surpluses can be treated as a derived demand from industrial expansion elsewhere; ie, chiefly the EU and Asia. Since growth in China is already very high, little more need be said other than to express some question about how long the current rate can be maintained. What of Japan and Germany? In Japan, after fifteen years of stagnation and five of deflation, a looser fiscal and monetary stance seems to be producing conditions favourable to sustained growth.⁴¹ By contrast, after five years of very slow growth in Germany, a slight improvement in performance in the past year appears to have produced dismay at the ECB, which in March 2006 raised its interest rate and is warning member-states once again against budget deficits.⁴²

In sum, 'Anglo-Saxon' growth has been driven by private spending sustained by rising asset prices. The role of Government has been confined largely to keeping interest rates low

⁴⁰ In 2006 the US trade deficit was \$765bn; see US Census Bureau, Foreign Trade Statistics, December 2006.

⁴¹ A complication is the inflow of hot money taking advantage of Japan's very low interest rates, one reason why the BoJ has recently raised its rate by a quarter of one percent.

⁴² See for example Irvin, G (2006); also see Goodhart, CAE (2006).

by capping public borrowing, and to promoting liberalised credit markets enabling holding gains to be converted to ready cash. Orthodox professional discussion has focussed on whether or not Government (particularly in the US) has been too discretionary in fiscal and monetary matters, about how and when to rein in irrational exuberance, about supply-side 'flexibility' and so on. Significantly, almost nothing has been said about the relatively low levels of productive (private and public) investment, the decline in manufacturing relative to financial sector activity and the growing household income dispersion accompanying the Anglo-Saxon consumer boom.

A Tax-based Solution?

The macro-economic scenario set out above is gloomy. Briefly, I have argued that growing overseas indebtedness mirrors growing household indebtedness, a phenomenon which growing income and wealth disparities have helped to fuel. Moreover, in the shorter term, any attempt to turn off the tap of consumer spending might fuel a recession---and a run on the dollar---which could seriously damage the world economy. In the longer term, clearly, any initiative which seeks to contain consumer spending and shift resources to the public sphere will need to bite the bullet of fiscal redistribution.

The conventional argument against fiscal redistribution is that since the rich save more, higher taxation would reduce total private savings and investment. In a closed economy, this is clearly nonsense since taxation redistributes resources to Government, which can then save and invest along traditional Keynesian lines. The problem is that in an open economy, the rich can shift their money abroad; ie, the redistribution of savings and investment is not between classes but within countries. The answer is twofold. First, some form of taxation is required on international capital flows. The Tobin-tax idea has been with us for many years and now has a number of variants, some of which have been successfully implemented. Second, there is growing inter-state co-operation on 'withholding taxes'; ie, pre-emptive taxes levied on capital seeking overseas sanctuary. The US already operates a withholding tax scheme and the EU has made considerable progress recently in the application of such taxes to offshore banking centres; there is no reason in principle why such an arrangement cannot be extended. However, successful action here requires considerable strengthening of fiscal co-operation between OECD countries.

Abstracting away from the problem of capital flight, there remains the 'crowding out' objection that increased personal taxation would merely lower household savings. A solution proposed by a number of economists, and most recently by Robert Frank⁴³, has been to replace personal income tax with a personal consumption tax. The mechanics are relatively simple; individuals in addition to declaring disposable annual income would declare annual savings and it is the difference (Yd-S) which would be taxed. In contrast to other writers on inequality, Frank presents clear proposals for a highly graduated consumption tax with a top marginal rate of 70%. The merit of such a tax, Frank argues, would be to soak the rich while scotching the argument that taxation reduces private savings.

Another egalitarian form of taxation which has been discussed for many years is a wealth tax; ie, a tax on the stock of private assets. One of its variants, the land tax, was famously proposed by the 19th century American writer, Henry George, and was favoured in

⁴³ See Frank, *op cit*.

the UK by early 20th century Liberals and, more recently, by Nicholas Kaldor. Marx's objections to Henry George notwithstanding, the case for some form of land tax in the UK stems from the relative importance of the landed aristocracy in the country's rich list.⁴⁴ More generally, however, Britain is one of the few EU countries which does not have some form of wealth tax.⁴⁵ At the same time, with the exception of France, other EU countries have tended to use a high threshold and a very low rate---typically less than 1%---with the result that its redistributive impact has been small.

Doubtless, the favoured instrument of redistribution remains the progressive income tax coupled with estate tax and other asset taxes. Although in the past 20 years top rates of income tax have come down in most OECD countries, Britain's top marginal rate is amongst the lowest of the EU-15 countries and Britain's overall tax incidence is regressive. In general, however, it is for political reasons that the system cannot be redesigned to make it more redistributive; if it bites the rich, the rich will bite back. This is as true of a steeply progressive consumption tax as it is of income tax, or indeed any combination of taxes on income and assets. At the same time, there is no doubt that the steeply progressive personal income tax regime which emerged prior to and following the Second World War was a major factor in shaping the household income distribution and keeping executive pay in check. As Michael Trotter has written of the USA:

[In] the Eisenhower years ... the top marginal rate of federal income taxation for married couples was 91 percent, and it kicked in at taxable income of \$2.7 million in 2006 dollars. Under these circumstances it is not surprising that most employers weren't willing to pay executives or anyone else great sums of money that just went to swell the federal government's tax coffers. Most employees didn't see much point in it, either. As a result, the income spread back then between the top "earners" and the rest of mankind was not nearly as wide as it is today. (Trotter, *loc cit*).

Conclusion

This paper has focussed on the political economy of the massive redistribution of income taking place in the Anglo-Saxon world since 1980. Contrary to the conventional narrative (including the New Labour version) about the benefits of 'meritocracy'⁴⁶ and achievements of a new entrepreneurial 'wealth creating' class, the argument presented here is that the new inequality brings growing political and social instability. At the heart of the analysis lies the decline of Anglo-Saxon economic competitiveness experienced in the 1960s and 1970s. The Reagan-Thatcher era was seen by some---including apparently Tony Blair and Gordon Brown---as ushering in a new, dynamic spirit of entrepreneurship unburdened by high taxes, rigid labour markets and wasteful public spending. Privatisation, coupled with a new, market-driven reward structure for high-fliers would re-invigorate capitalism in its heartland.

⁴⁴ A handful of aristocratic families, starting with the Grosvenors, own most of London's most valuable real estate and regularly figure at the top of the annual rich list published by *The Times*. See Lansley (2006) Chap 5. On a land tax for the UK, see A Seager 'A land tax is 200 years overdue' *The Guardian*, 8 Jan 2007.

⁴⁵ In 2000, the following EU member states levied a wealth tax: Austria, Denmark, France, Germany, Greece, Luxembourg, Spain, Sweden, and The Netherlands.

⁴⁶ A particularly trenchant critique of the New Labour notion of 'meritocracy' is Barry (2005).

In truth, the industrial position of the US and the UK, far from improving, has worsened. The growth of the financial services sector and restructuring of corporate manufacturing has fuelled growing inequality and a debt driven consumption boom. These phenomena feed on each other, as the ladder of aspirational lifestyles stretches ever further upward. As the rich fight to become very rich, the middle class finds its footing on the ladder ever more precarious, skilled public service workers cannot find houses near their jobs, semi-skilled workers find can't make ends meet and a new 'permanent' underclass emerges which can no longer aspire to getting anywhere near the base of the ladder of opportunity, still less to climbing its lower rungs. For the majority, the 'new economy' means more hours worked per year, more working family members, later retirement on meaner pensions and greater unsecured debt. The social costs of growing inequality have been carefully documented by writers like Frank, Putnam, and Wilkinson; in a phrase, inequality seriously damages social health.

The macro-economic implications of all this affect both the developed and the developing world. If the negative savings of US and UK households outweighs all forms of positive domestic savings, investment and growth in the Anglo-Saxon world must be financed by high savings rates in the developing world. As a recent paper on global imbalances puts it:

Current global imbalances not only pose huge dangers; they also cause a grossly inequitable distribution of global resources. Capital is 'flowing uphill' to rich countries—overwhelmingly to one rich country, the US. A stark illustration of this inequity: the average US current account deficit in recent years has been one third higher than the total Gross Domestic Product of sub-Saharan Africa.⁴⁷

Although UK growth is more closely related to financial services than its US counterpart, in both countries a slowdown appears imminent and indeed is already evident in the US. While a 'soft landing' for the dollar may appear more likely today than a year ago, financial sentiment is notoriously volatile and a major run of the dollar would almost certainly precipitate a major world recession. There is little reason to suppose that widespread recession would not accelerate the growth of inequality both within and between countries.

Assuming that recession is avoided, can the growth of inequality in the Anglo-Saxon world be reversed? The answer must in principle be 'yes', but the solution requires a return to levels of direct taxation not seen for 30 years---and probably strict new measures by government to regulate the inter- and intra-generational distribution of assets. Given the current absence of countervailing power to the super-rich who, increasingly, are able to buy public institutions and sway political opinion, it is difficult to be optimistic.

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⁴⁷ See McKinley, T and A Izurieta 'The Gross Inequities of Global Imbalances' *International Poverty Centre, UNDP*, Feb 2007, No 30.

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Science, ideology and development: Is there a 'Sustainability Economics'?

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Abstract

The reasons why we as scholars prefer one paradigm to another are not only scientific but also ideological. It is suggested that pluralism should be discussed at the levels of theory of science, paradigms in economics and ideological orientations. Neoclassical economics is closely connected with logical positivism as a theory of science and is close to Neo-liberalism as an ideological orientation. Specific ideas of institutional arrangements follow from these perspectives. Alternatives to the mainstream have similarly to be articulated and discussed at all three levels to open the door for an alternative set of institutional arrangements.

Exclusive reliance on economic growth in GDP-terms and on monetary profits exemplifies an ideological orientation. When faced with new challenges such as Sustainable Development and Corporate Social Responsibility, the shortcomings of the neoclassical paradigm become accentuated. Alternative ideas to those of Economic Man, profit-maximizing firms and the mechanistic model of markets in terms of supply and demand are needed. A political economics approach to an understanding of individuals and organizations as actors in markets and institutional change processes is proposed.

Introduction

Mainstream neoclassical economics is attacked by many and from different angles or vantage points. Neither the defendants nor the critics can claim value-neutrality. "Values are always with us" (Myrdal 1978) and economics is always 'political economics'. The neoclassical attempt to construct a 'pure' economics has failed. Neoclassical theory may still survive as a theory that is specific in scientific and ideological terms and useful for some purposes. But this survival has to be accompanied by the admission that neoclassical theory is built on assumptions that are specific in terms of ethics and ideology and that alternatives to these assumptions exist. The future of neoclassical theory is therefore not only a matter of its usefulness to solve economic problems in some sense but also has to do with the ideological preferences of scholars who have become accustomed to neoclassical theory and of other actors in society who may exploit neoclassical theory for their own purposes. Vested interests are involved and in neoclassical language one may argue that even when the conceptual weaknesses are demonstrated and understood there may still be a considerable 'demand' for neoclassical theory.

The vision of one logically closed economic theory for all purposes has to be abandoned in favour of an idea that different theories are useful for different purposes and that attempts to reduce these different theories to one single Master theory are no longer meaningful. In a democracy, the continued existence of competing and complementary theories, reflecting different ideological points of view is a necessity and is even positive for the development of economics as a discipline. Monopoly for one theory is not conducive to new thinking and creativity. 'Competition' may sometimes be good for individuals and for society at large, to once more use a neoclassical vocabulary.

One often hears actors argue in ways suggesting that Western societies are democracies by definition. But even if these societies perform well in some respects it is equally true that all 'democracies' can be strengthened. The existence of monopoly for neoclassical theory at Departments of Economics all over the world exemplifies an element of 'dictatorship' that cannot be accepted and has to be replaced by competition and pluralism.

In this paper I will focus on the challenge of getting closer to Sustainable Development as a justified purpose for economic theory and analysis. Neoclassical theory may not be completely useless for this purpose but the ideology built into neoclassical theory certainly goes against any reasonable interpretation of Sustainable Development. This will be further elaborated in the pages to follow.

Interpretations of Sustainable Development

Sustainable Development (SD) is a 'contested concept' (Connolly 1974). In social science one has to live with contested concepts like power, freedom, interest, ideology, democracy and this is not necessarily a disadvantage. The existence of more definitions and opinions than one is a starting point for dialogue and clarification. And clarification of different points of view may lead to new thinking. I will here point to three conceptual and ideological interpretations of SD:

- Business-as-usual. For some actors SD does not mean anything new. It may refer to 'sustained economic growth' in GDP terms at the national level and 'sustained profits' in business corporations
- Ecological and social modernization. Here it is believed that present challenges to sustainability can be dealt with through modification of the present political economic system. Minor social and institutional change processes are encouraged provided that they do not threaten essential structural aspects of the present political economic system.¹ Environmental charges or taxes, environmental labelling, Environmental Management Systems, voluntary codes of conduct in business are examples of such minor institutional adjustments.
- More radical transformations of institutional arrangements. SD is then understood as an essentially multidimensional and ethical concept. In addition to 'modernization', radical changes in political economic system have to be considered to counteract present unsustainable trends. It is not easy to state more precisely what those institutional changes should be but we can start by referring to the values or ideological orientation that could guide us in the transformation process.

Sustainable Development became part of the international development dialogue through the work of the World Commission on Environment and Development. Many actors and voices contributed and its report is partly contradictory (WCED, 1987). Arguments about "vigorous economic growth" are mixed with pleas for environmental protection and an understanding of a common destiny at a global level. It is however important to note that the mentioned Brundtland report and the following UN-process connected with the Rio des Janeiro conference in 1992 claimed some 'newness'. I suggest that this new emphasis in development thinking brings together at least four elements:

¹ This suggests that there is a business-as-usual aspect also in this interpretation of SD but at a different level.

- A movement away from exclusive reliance on monetary ideas of progress in business and society to an *emphasis on non-monetary considerations* concerning health, equality, employment, culture, environment etc. Climate change exemplifies an urgent issue where irreversibility is present. Later the UN Millennium Development Goals (United Nations 2005) has made this emphasis on non-monetary performance more concrete. And this spectrum of non-monetary factors and impacts is not reducible to money or any other 'common denominator'.
- A movement away from narrow and short-sighted ethical considerations to an effort to *extend horizons in time and geographical terms*. The title of the Brundtland report "Our common future" suggests that when considering options in some specific region, actors should broaden their ideological orientations. Institutional arrangements should be designed to also consider impacts upon people in other regions and upon future generations.
- The use of chemicals (and technology more generally) has to be carefully scrutinized and a *precautionary principle* observed. In a report from the European Environmental Agency with the subtitle "Late Lessons from early warnings", a number of cases of 'technological optimism' where the precautionary principle was not observed are described (Harremoës et al. editors 2002). Thinking in terms of prevention and security are closely related imperatives.
- The Rio process also pointed to the role of *democracy* and dialogue as part of its Agenda 21 documents. SD is not exclusively a matter for an existing technocracy or a new elite. As many actors as possible should participate with their different backgrounds, roles, ideas and interests.

Neoclassical theory in relation to SD

Neoclassical economics is certainly conceptually and ideologically compatible with the 'business as usual' interpretation of SD. Economic growth in GDP-terms is the main indicator of progress at the macro level and monetary profits in business at the micro level. But if SD is (conceptually and ideologically) interpreted in terms of 'modernization' plus 'radical change' or along the lines of a 'reasonable interpretation' above, neoclassical economics has little to offer.

In 2003 the Ministry for research and education in Germany turned to one of the more established neoclassical economics research institutes, DIW (Deutsches Institut für Wirtschaftsforschung), Berlin, arguing that neoclassical economics is 'inadequate' for sustainability issues. What is needed is a 'sustainability economics'. Actors within DIW then initiated a number of workshops in an attempt to overcome these limitations (www.sustainabilityeconomics.de).

As will be further elaborated, neoclassical Economic Man assumptions do not respond well to the need to extend horizons and problematize the ideological orientation or ethical aspects of human thinking and behaviour. The assumptions behind the theory of the firm, especially its 'monetary reductionism' do not facilitate an increased understanding of issues such as Corporate Social Responsibility or the existence of Environmental Management Systems such as ISO 14 001. Neoclassical market theory is about supply and demand in mechanistic terms and does not raise ethical issues of 'fairness' and 'exploitation' as possible characteristics of relationships between market actors. Neoclassical international trade theory efficiently cuts off categories of impacts that are important for many actors and interested

parties. Cost-Benefit analysis exemplifies 'monetary reductionism' and a kind of 'ideological correctness' by assuming that we all agree about correct prices to be applied for purposes of resource allocation.

At a macro level, the simplifications and ideological tendencies in neoclassical theory legitimize the present role and dominance of big corporations, so called 'corporate globalization' (Korten 2001, International Forum on Globalisation, 2002, Shiva 2006) and are also behind the present global competition between regions. This competition may be good for some purposes but is increasingly causing stress to human beings and ecosystems. Natural resources are systematically degraded in the name of progress. To summarize, neoclassical economics legitimizes a worldview and ideological orientation that now appears to be an essential part of the problems faced.

Different kinds of pluralism

In the development debate there are those who want to go directly from observations in the field about negative trends in environmental or social terms to measures with a presumed potential to counteract such trends. In what follows, it is argued that it is wise to also consider options at the level of perspectives and thinking patterns. As an example, the comparison between neoclassical and institutional economics has to be seen in a broader context of competing perspectives. Also theory of science is involved where alternatives to positivism exist (Table 1). Similarly one cannot avoid discussing competing ideological orientations if one wishes to take the present sustainability challenge seriously. It is a big mistake to regard the issues of values, world view and ideology as exclusively a matter for politicians. Efforts are needed to *illuminate* such issues rather than avoiding them. This suggests that there is an issue of competition and pluralism at different (and interrelated) levels:

- theory of science and the role of science in society
- paradigms in economics and business management
- ideology and the ideological orientation of actors, especially those in power positions
- institutional arrangements that largely follow from the choice made among previously mentioned options.

In Table 1 dominant (or mainstream) perspectives are compared with complementary or alternative perspectives. The point here is that the dominant perspective in theory of science is closely related to the dominant perspective in economics which in turn is close to the dominant ideological orientation. As suggested to the left in Table 1, positivism is behind neoclassical economics and neoclassical economics is rather close to neo-liberalism and a business as usual interpretation of SD. Not only neoclassical economics but all three perspectives tell us something about the kind of institutional arrangements that we see today.

The right hand side of Table 1 suggests that ideas about good science are not limited to positivism. Various forms of subjectivism have gained legitimacy such as social constructivism (Berger and Luckman 1966), hermeneutics (Ricoeur 1981), narratives (Porter Abbott 2002), discourse analysis (Fairclough, 1995), contextualism (Toulmin 1990). We can learn from listening to the stories told by professional and other actors related to specific sustainability issues, for instance. How do they interpret SD and how does this interpretation influence practical behaviour? Have they at all internalized the concept of SD or do they stick to a business as usual interpretation? In terms of ideological orientation, the alternatives to

neo-liberalism are many but let us think of priority for environmental, health and social considerations. For institutional arrangements, an alternative is to refer to a 'subsidiarity principle' (International Forum on Globalization 2002). This principle is regarded as essential also in the rhetoric of the European Union. While not denying important global interactions, local societies and local market relationships and 'nearness' to actors with power should be strengthened when compared with 'absentee ownership'.

Table 1. Overview of fundamental perspectives in relation to a dialogue about Sustainable Development.

| | Dominant perspectives | Complementary or alternative perspectives |
|--|--|--|
| Theory of science; role of the scholar in society | Positivism; expert standing outside | Subjectivism, social constructivism, hermeneutics, contextualism; concerned scientist |
| Paradigms in economics | Neoclassical | Political approach to institutional economics |
| Ideological orientation | 'Business as usual' interpretation of SD. Extreme market ideology; GDP-growth, reductionist ideas of efficiency, preference for privatisation (neo-liberalism) | 'Modernist' or 'radical' interpretation of SD. Priority for Social, Health and Environmental (SHE-) aspects as part of a holistic judgement |
| Institutional arrangements | Institutions that facilitate for 'corporate globalization' e.g. the present World Trade Organization (WTO) | Subsidiarity principle; Local community development and local markets as starting points. A World SHE-organization "to handle trade disputes" at the global level. |

Table 1 should not be understood in a traditional sense as one perspective or set of perspectives being scientifically correct or 'true' while the other perspectives are false. Even perspectives on the left hand side have a role as part of a pluralistic philosophy. For some kinds of problems, neoclassical economics may be useful (monetary policy, for instance). But for the kind of problems that interest us here neoclassical economics will play a secondary role or even be part of the problems faced. The 'fact' that ideological orientation is involved means that it is not realistic in a democracy to limit attention to one scientific and ideological perspective. Actors within Department of Economics make this mistake and these departments thereby play a role as political propaganda centres.

Options with respect to theory of science

While there is interdependence between levels in Table 1, it is still meaningful to take a look at each level. Looking first more closely at tensions between perspectives referring to theory of science (Table 2), neoclassical theory is essentially based on positivism while institutional economics brings in more subjectivist manners of doing research, such as social constructivism, hermeneutics and narrative analysis. With respect to time, neoclassical theory is mechanistic with 'static' and 'comparative static' analysis while institutional economics

tends to be evolutionary referring to concepts such as inertia, path-dependence and irreversibility.

Table 2. Tensions between dominant perspective and alternative perspectives with respect to theory of science.

| | Dominant perspective (Positivism) | Alternative perspectives (social constructivism, hermeneutics, narrative analysis etc.) |
|--|---|---|
| Time aspect | History not important; mechanistic models | History matters; evolutionary patterns, path dependence |
| Value issues | Objectivity, value-neutrality | Subjectivity matters; dealing with values and ideology in a conscious and open way |
| Field of inquiry and position in relation to it | Standing outside observing events; traditional role as expert | Entering into a dialogue of interactive learning with actors and interested parties |
| Purpose of study | Looking for universal regularities | Case studies, uniqueness, contextualism |
| Methodological guidelines and habits | Quantification, optimal solutions e.g. the 'monetary reductionism' of CBA | Illumination of options with respect to ideological orientation and impacts of alternatives; conditional conclusions e.g. disaggregated and ethically open analysis in terms of Positional Analysis, PA |
| Decision-making | Decisions essentially based on calculation by experts | Matching ideological orientation of each decision-maker and expected impacts of each alternative; 'appropriateness', 'pattern recognition' |

In the neoclassical approach, the analyst is an outside, disengaged observer aiming at objectivity and value-neutrality. The institutional analyst – the right hand side of Table 2 – recognizes his own subjectivity as important and influential in the research process. He also takes an interest in the subjectivity of other actors and interested parties, listens to their narratives etc. The scholar typically enters into a dialogue with other actors as part of an interactive learning process.

While the neoclassical economist typically looks for regularities, even laws of corporate conduct, the institutional analyst is ready to consider each case as unique, partly based on specific contextual factors. As already indicated, positivism is the main theory of science for neoclassical economists. Qualitative analysis may be used but quantification is the ideal. Cost-Benefit Analysis, CBA, is based on the assumptions that decision-makers need clear-cut one-dimensional numbers, that money is the best measuring rod and that it is meaningful to refer to correct prices for specific impacts. Experts point to optimal solutions and it is expected that politicians or other decision-makers will listen to advice of this kind from experts.

The alternative to optimization is 'illumination' of an issue in a many-sided way for actors and interested parties who differ among themselves with respect to position, interests and ideological orientation. This approach is based on normal imperatives of democracy. Dialogue, sensitiveness to opinions other than your own and interactive learning are some characteristics of this process. But there is also an effort to systematically deal with

ideological orientations, alternatives of choice and impacts. Conclusions are conditional (in relation to ideological orientation and scenarios about the future). Positional Analysis (PA) is the approach to Sustainability Assessment, or more generally decision-making, preferred by the present author.

While neoclassical economists typically focus on things going on in ecosystems or the 'field' more generally, an institutional economist may focus on actors and their understanding of concepts such as 'Sustainable Development'. In the Uppsala and Kalmar regions in Sweden, new organizations have been set up for planning at the regional level and actors involved in these activities have been approached with questions about what they see as the main objective for their activities, how they understand the concept of sustainable development and how this understanding influences their practice. With few exceptions the result was that 'economic growth' and 'international competitiveness' are the big things while health, social considerations and environment are secondary issues (Puskas Nordin, 2004). It may be added that dialogue with neoclassical economists or institutional economists are equally meaningful as part of an interactive learning process (Borgström Hansson 2003). The idea is to make the respondents responsible as actors and their arguments visible.

Options with respect to paradigms in economics

Institutional theory as an alternative to neoclassical economics, its microeconomics in particular, has been presented elsewhere (Söderbaum 2000). This attempt to develop an economics more appropriate in relation to Sustainable Development continues. A 'Sustainability Economics', 'Ecological Economics' or 'Green Economics' is very much needed. The present version by no means excludes contributions from other schools of thought and authors.

Here I will focus on three aspects of such a sustainability economics. Individuals and organizations are understood as actors in a political context. Markets are understood as part of an actor-oriented approach. Decision making and *ex post* evaluation or Sustainability Assessment is discussed in a multi-dimensional, ideologically open way compatible with normal imperatives of democracy.

Political Economic Persons and Political Economic Organizations

In Table 3, neoclassical Economic Man assumptions are compared to a view of the individual as a Political Economic Person (PEP) i.e. an individual as actor guided by her 'ideological orientation'. I will here assume that my readers are reasonably acquainted with Economic Man assumptions and focus on the right hand side of Table 3.

The Economic Man interpretation of individuals is based upon assumptions about preferences, alternatives and impacts as given. It is a closed model that lends itself to simplistic mathematical treatment. The PEP-model on the other hand is more open. The individual refers to her ideological orientation but this orientation as well as alternatives of choice and impacts are more or less fragmentary and uncertain. The individual's preferences may be changing over time and the same is true of information about alternatives and their impacts. The individual is learning while interacting with a changing context.

Table 3. Two schemes of interpretation: Economic Man versus Political Economic Person

| | Economic Man | Political Economic Person (PEP) |
|----------------------|---|--|
| History | Not considered relevant | The individual is a product of her history and her relationships to specific contexts; path dependence |
| Context | Markets for products and factors of production | Political, socio-cultural, institutional (e.g. market), physical man-made, ecological |
| Roles | Consumer, wage-earner | Citizen, parent, professional, market-related roles etc. |
| Relationships | Market relationships between selfish market actors | Market and non-market relationships of a cooperative or non-cooperative kind |
| Values | Maximum utility of commodities within budget constraint | Ideological orientation as guiding principle e.g. 'Green' orientation |
| Behaviour | Optimizing | Habitual, 'rule-following', also learning and conscious choice (decisions); appropriateness, matching |

Source: Söderbaum 2001 p. 187.

Reference is made to concepts from social psychology, such as role, motives, identity, dissonance, relationships and activities. The individual as actor disposes of certain resources at a particular point in time and can use her power position for different purposes. As citizen and in other roles she can articulate her ideological orientation and change her life-style to make it more compatible with Sustainable Development, for instance. She also influences other individuals by her example and in other ways.

'Political' in 'Political Economic Person' stands for the fact that our societies claims to be democracies. The individual is expected to respect a number of imperatives of democracy. As actor the individual is a responsible and accountable person in her different roles as citizen and professional. There is a private sphere but the behaviour pattern or life-style of an individual is at the same time a political issue, i.e. an issue that concerns others. We all understand, for instance, that the choice of means of transportation has impacts upon other individuals, sometimes even at a global level.

While neoclassical theory focuses on business companies or firms, the term Political Economic Organizations (PEO) suggests that also other organizations, such as environmental organizations, human rights organizations, churches, universities, political parties, think tanks (and even research organizations such as the International Confederation of Associations for Pluralism in Economics, ICAPE) can be of interest in relation to the challenge of Sustainable Development. Business corporations take part in this dialogue about the future, sometimes openly, sometimes by attempting to influence other actors such as representatives of national governments or the European Union. Some business companies refer to their Corporate Social Responsibility (CSR), phenomena that much like other ethical considerations, can hardly be understood within the scope of a neoclassical paradigm.

Table 4. Organizations: the neoclassical and institutional view

| | Profit-maximizing firm | Political Economic Organization (PEO) |
|---|---|---|
| History | Not considered relevant | The organization is a product of its history; path-dependence |
| Context | Markets for products and factors of production | Political, socio-cultural, institutional (e.g. market), physical man-made, ecological |
| Justification for existence | Profits for shareholders | Business concept, mission statement, 'Core Values', political ideology, 'social responsibility' |
| View of individual | Largely invisible | Polycentric organization with individuals as PEPs, guided by their ideological orientation |
| Relationships | Internally: largely invisible, hierarchic Externally: market relationships | Interaction (cooperative and non-cooperative) between individuals as actors, internally and externally, market and non-market |
| Interests related to corporation | Consensus idea based on assumed shareholder values | A complex of common and conflicting interests between stakeholder categories and individuals as actors |
| Decision act | Optimization: maximum profits | Multidimensional impact studies, also rule following, matching ideology (mission statement) with expected impacts |

The PEO is 'polycentric' in the sense that each individual is a Political Economic Person (PEP) and that the ideological orientation of a member of the organization may depart more or less from the objectives and visions of the leadership. Such tensions can be constructive for the success of an organization and even lead to a reconsideration of its mission.

Relationships between market actors

While neoclassical theory focuses on and is limited to market relationships, the kind of institutional theory presented here also recognizes the existence of 'non-market relationships' as important in the development dialogue and practice. But let us focus on market relationships since they are at the heart of neoclassical economics. Are there alternatives to supply and demand?

As part of the institutional perspective, market relationships are no longer exclusively understood in mechanistic terms but also in social and evolutionary terms. Market actors are individuals (and this is so even when they work for organizations) who may bother about each other or (influenced by the neoclassical perspective) see a particular relationship as completely impersonal.

Table 5. The market as a phenomenon. Two schemes of interpretation

| | Neoclassical perspective | Institutional perspective |
|---|--|---|
| History | Not considered relevant | Each market relationship has its history that may or may not involve trust, commitments etc. |
| View of individual | Economic Man | Political Economic Person as actor |
| View of organization | Profit maximizing firm | Political Economic Organization as actor |
| Interaction between buyer and seller | Supply and demand | Multifaceted social relationship between potentially responsible market actors |
| Goods and services | Homogeneity, one commodity at a time | Also heterogeneity, multiple commodities and transactions, multi-functionality in relation to many interests and stakeholders |
| Motives for transaction | Profits or utility related to quantity and price (optimization) | Ideological considerations 'monetary price and beyond' (matching) |
| Relations to other actors | Emphasis on personal gain (Belief in 'invisible hand') | Also inclusive ('I & We Paradigm', 'Person in Community') |
| Features of relationship | Independence: contracts between parties with conflicting interests | Also cooperation; considerations of trust and fairness |

Market actor A may exploit her power position in relation to Market actor B or think in terms of common interests and fairness. 'Trust' is known to be an important factor in 'business to business' relationships (Ford 1990). As with other social relationships an ethical aspect is present and judgments of fairness are not limited to prices but may refer to all kinds of conditions and impacts. In the case of 'corporate globalization' also impacts related to culture, health and environment are involved. A transaction is furthermore often part of networks of relationships between multiple actors rather than limited to two parties.

Neoclassical market theory, especially international trade theory, has influenced the design of international institutions, such as the WTO (World Trade Organization). When it is argued that this theory contributes to increased efficiency in the global economy and improved welfare for all, it should be understood that reference is made to an efficiency concept that is specific in scientific as well as ideological terms. This ideology is shared by many professional actors once educated in neoclassical economics, for instance the Trade Commissioner Peter Mandelson of the European Union and Thomas Östros, the previous Trade Minister of Sweden. Their reasoning in relation to quotas on shoes and textiles for the European Union is extremely simplistic. What is called 'free trade' is good, 'protectionism' is bad. ²It can be added that Östros came directly to politics from the Department of Economics, Uppsala University.

² But 'protecting' neoclassical theory from competing ideas is good.

This neoclassical trade theory focuses on one dimension, i.e. the price at which a commodity can be delivered and is extremely narrow in cutting off a large number of other considerations about impacts on employment in different parts of the world; about environmental impacts and on culture. Ethics is not part of this idea of rationality. The international trade theory is rather of a cynical kind. But it may still suit some actors and interested parties.

Today climate has become an issue. When faced with this, leading politicians, civil servants, scientists equipped with their market fundamentalism naturally think in terms of market solutions. In this way we have got the Kyoto protocol with its many flexible (escape) mechanisms. Larry Lohman at the Corner House in UK has articulated what many feel in the book *Carbon Trading* (Lohman 2006). Among other things, he focuses on the impossibility of knowing and quantifying what would have happened without a specific project within the scope of the CDM:s (Clean Development Mechanisms).

Approaches to Sustainability Assessment and decision making

As we all know Cost-Benefit Analysis (CBA) in monetary terms is the approach to decision-making at the societal level advocated by neoclassical economists. Money is the measuring rod and the idea is to transform all impacts that are non-monetary in kind to their alleged monetary equivalent. The prices used for this operation are current market prices and for the case that an actual market does not exist, imagined (or hypothetical) market prices. 'Revealed preferences', 'contingent valuation' are parts of the vocabulary used when finding out what the 'correct' prices are from the point of view of optimal 'resource allocation'.

Over the years there has been a debate about the claims of CBA advocates that theirs is 'the' approach to decision-making. Even persons essentially educated in the neoclassical tradition occasionally raised their doubts. Ezra Mishan wrote a textbook on CBA (1971) but later argued that CBA can be used in a particular society only if there is a consensus in society about the rules of valuation built into the method. Mishan was concerned about environmental issues and considering the conflicting views about environmental issues at the time, he argued, that such a consensus (if it had existed earlier) no longer existed (Mishan 1980).

Mishan did not use the word 'ideology' but his observation and judgement can be reformulated by saying that CBA is based upon a specific ideology and one that is more precise than other ideologies, for instance liberalism and social-democracy among established political ideologies. Another mainly neoclassical economist, Leif Johansen, identified the CBA-ideology as being close to, if not identical with, the 'economic growth' ideology (Johansen 1977). The conceptual framework is the same and the logic in terms of 'net present value' is similar to the 'net value added' concept used in GDP accounting exercises.

The debate between the advocates of CBA (e.g. Sunstein 2002) and critics (e.g. Ackerman and Heinzerling 2004) will continue. CBA advocates get political support from those educated in neoclassical economics and from neo-liberals. The future of CBA is not only a matter of good science but also of 'political demand'.

Today many of us are critical about the economic growth ideology and we look for ideological openings in Green or other directions. We live in democracies and therefore

approaches to decision-making should be ideologically open rather than closed. An issue should be *illuminated* in relation to different possible ideological orientations that appear to be relevant. Rather than reference to the 'optimal' solution we should refer to 'conditional conclusions' in relation to each ideological orientation considered and other assumptions made. A Green ideological orientation, specified in some way, will in many cases point to other alternatives than a 'business-as-usual' orientation (e.g. an economic growth orientation) as appropriate.

Alternatives to CBA should then be less technocratic and more compatible with democracy. Such a move also suggests that the analyst should engage in a dialogue and interactive learning process with interested parties and other actors; what are their positions in relation to the issue? How do they understand the problem? How do they articulate their ideological orientations in a more narrow sense and for society at large? What do they expect in terms of impacts for the case that specific alternatives are chosen?

The existence of more than one ideological orientation in relation to an issue suggests that aggregation in one-dimensional terms is not a useful strategy. Rather one has to distinguish between different kinds of impacts and think in terms of multidimensional profiles. In Table 6, a distinction is made between monetary and non-monetary impacts and another distinction between impacts expressed as 'flows' i.e. for specific periods of time and impacts expressed as 'positions' or states, i.e. for specific points in time.

Table 6. A classification of impacts in economic analysis.

| | Flow (referring to a period of time) | Position (referring to a point in time) |
|---------------------|---|--|
| Monetary | a | b |
| Non-monetary | c | d |

The turnover of a business company and the salary of a person employed exemplify monetary flows (a. in Table 6). The balance sheet is a monetary position (or set of monetary positions, if you prefer – cf. b.). Pollution from a factory or transportation activity is a non-monetary flow (c. in Table 6) and the existence of some pollutants in the blood of a human being at a point in time, a non-monetary position (cf. d.). Land-use changes, changes in available knowledge and in health are often described in positional terms.

The idea here is that non-monetary impacts should be described in their own terms. Environmental Impact Statements and Environmental Impact Assessment (EIA) builds on a similar idea that environmental impacts should be considered separately and not 'disappear' by being mixed up with monetary impacts. While EIA is a disaggregated approach that distinguishes between different environmental consequences, the EIA procedure may have some disadvantages and limitations. It does not cover all kinds of impacts and generally enters into the decision process too late when the project owner is committed to one alternative and knows what he or she wishes to accomplish (cf. Söderbaum 2004a).

The preference of the present author is Positional Analysis (PA) suggesting that 'positional thinking' in non-monetary terms, is a good idea. Positional thinking is thinking in two or more steps where decision trees can be used and aspects such as inertia and irreversibility illuminated. A decision is normally regarded as a first step leading to new

positions (with new options) that differ qualitatively from previous positions, much like the way a game of chess develops.³

Monetary impacts may be considered in a step by step fashion but this way of looking upon decision-making and decision processes is perhaps even more relevant on the non-monetary side. If specific ecosystems are exploited for construction purposes then it is not so easy to return to the previous position in land-use terms. Today we learn about the impacts on climate in different parts of the world from CO2 emissions connected with transportation, for instance. Exploitation in the form of mining or dam construction often leads to resettlement of indigenous people, another ethical issue not so easily solved through monetary calculation.⁴

Options with respect to ideologies and ideological orientations

If economics is political economics then politics is no longer outside economics. Even articulation of ideological orientation and 'ideology development' become central concerns. What are the desired directions of change? How do we describe the ideology that is dominant in Western societies and what are the alternatives?

Since the dominant ideology in Western societies is so much connected with neoclassical economics, it can be expected that there is a need for a new economics, a Green economics if one wishes, to strengthen Green ideology. Something has hopefully been achieved in this respect in previous pages. I will here focus mainly on neo-liberalism and the relationship between neoclassical economics (as science and ideology) and neo-liberalism. In attempting to expose the weaknesses of neo-liberalism we will automatically get an idea of alternatives that are more constructive in relation to Sustainable Development (SD).

The International Forum on Globalization (2002) with authors such as David Korten, Vandana Shiva, Maude Barlow, Walden Bellow, Edward Goldsmith, Helena Norberg-Hodge has identified the following 'key ingredients' of neo-liberalism, alternatively called 'corporate globalization' (Ibid. p. 19):

- Promotion of hypergrowth and unrestricted exploitation of environmental resources to fuel that growth
- Privatization and commodification of public services and of remaining aspects of the global and community commons
- Global cultural and economic homogenization and the intense promotion of consumerism
- Integration and conversion of national economies, including some that were largely self-reliant, to environmentally and socially harmful export-oriented production
- Corporate deregulation and unrestricted movement of capital across borders
- Dramatically increased corporate concentration
- Dismantling of public health, social, and environmental programs already in place

³ It should be observed that unlike the decision trees used in game theory no quantitative 'pay-offs' are indicated at the end of the ramifications. Instead, each new position is qualitatively and quantitatively described with all its new possibilities.

⁴ It is not possible here to describe PA in detail, where the approach comes from and how it can be used, see Söderbaum 2000 pp. 85-105, Söderbaum 2006, 2007.

- Replacement of traditional powers of democratic nation-states and local communities by global corporate bureaucracies

In short, this is not a nice ideology or ideological orientation for many of us. But it may be useful in searching for and articulating alternatives. Let us first take a look at the relationship between neoclassical economics and neo-liberalism.

It has already been argued that neoclassical economics is not only science but at the same time ideology. Neo-liberalism is more extreme as ideology – a kind of market fundamentalism – but it is interesting to observe how many similarities there are between neoclassical economics as ideology and neo-liberalism (as ideology).

- There is a focus on markets in both cases and concerns outside the market receive only limited attention
- Economic growth in GDP-terms is the main indicator of progress in society in both cases
- The only organizations seriously considered is the firm or business corporation in both cases
- The consumer is the king and the consumer is supposed to consider only short run utility rather than bother about what is now referred to as sustainability (impacts upon others, future generations etc.) In both cases we are dealing with an ideology of 'consumerism'
- The focus is narrow in both cases in the sense of referring to one commodity at a time when dealing with markets and international trade. Reasoning in terms of multiple transactions, multiple interests, multi-functionality is avoided.
- Analysis is largely monetary in kind as in the case of CBA. Even neoclassical environmental economics emphasizes markets and the monetary dimension
- The efficiency idea is the same in both cases, referring to the monetary cost of each unit of a commodity produced, sold or bought.
- The simplistic nature of international trade theory means that this theory supports export-oriented production at the expense of local self-reliance
- Neoclassical economists similarly tend to believe that unrestricted capital movements across borders is good for efficiency in a global perspective

But neoclassical economics need not be as repugnant as neo-liberalism in some other respects:

- While neoclassical analysis is of little help in opening the doors for alternative ideas about efficiency, neoclassical economists are not necessarily in favour of privatisation
- While being silent about power issues, neoclassical economists need not support the uncontrolled growth of business corporations. They believe in competition as more efficient than monopolies and cartels
- Among neoclassical economists there are many social democrats (at least in Sweden) that are in favour of a strong state and who argue that there is still a role for regulation

While there is no complete identity, this comparison between neoclassical theory and neo-liberalism suggests that neoclassical theory conceptually and ideologically in many ways legitimizes neo-liberalism. It should always be remembered that thousands and thousands of students all over the world each year are indoctrinated in the belief system of neoclassical economics. Together with the activities of neo-liberal think-tanks, the dominance of market

ideology in present societies is not unexpected. Many professionals and political leaders do not know of any other economics.

Options with respect to institutional arrangements

Social and institutional change processes occur all the time from the micro level of individuals and organizations up to the national, European Union and global levels. At issue is whether these changes go in a Green direction or if unsustainable trends continue.

Ideas and ideological orientations play a role in this and so does science and conceptual models of various kinds. In the development dialogue, economic growth – now regional economic growth – is still the dominant objective in a country such as Sweden. A lot of money is spent in the search for individuals with ideas about how to start new businesses, so called entrepreneurs. Gender issues may enter into this process. Minorities such as immigrants are regarded as potential entrepreneurs and expected to contribute to economic growth, employment and prosperity. In our present society we are rather left with persons or actors who think in terms of neoclassical models and business management models that often are not much better. How can this be changed? Is it possible to increase the share of transformations towards sustainability?

These days we need ideas, models of change and even ‘Green entrepreneurs’ moving us towards sustainability although one does not hear so much about the latter. A first step is to try to understand social and institutional change processes. Here we enter into the whole fabric of social psychology and social sciences with learning theory and many other things. As always in science, some simplifications are necessary. Let us take the example of Environmental Management Systems, EMS. Business companies or firms have historically largely been understood in terms of the neoclassical model of profit-maximization. At some stage, a stakeholder model of business investments and operations entered the scene and modified the previous understanding. According to this perspective at least some conflicts of interest become possible in relation to the business corporation. Not only shareholders but also those employed hope to improve their monetary conditions, for instance.

As a result of public debate about environmental degradation, some business actors understood that ‘good business’ in present society is not only about monetary performance. There are various forms of non-monetary performance as well, such as environmental performance. Just as there are financial management systems, there could be environmental management systems. And to make such systems more legitimate and established, a kind of certification scheme with connected auditing organizations were needed.

Environmental Management Systems, such as ISO 14 001 and EMAS (European Union Eco-Management and Audit Scheme), have been discussed critically by many (e.g. Welford 1996). On the positive side, it can be argued that it represents a first step in a Green direction. EMS is an ‘institution’ in itself that will increase or decrease in prevalence over time. The interesting thing, however, is that much like the stakeholder model, it may change the understanding of a ‘firm’ or ‘business corporation’ as an ‘institution’ for some of us.

From a Green point of view, it is essential that individuals as actors are open for new interpretations of various phenomena. I like here to cite Willis Harman:

“By deliberately changing the internal image of reality, people can change the world” (Willis Harman, from Korten 2001, p. 233)

Institutional change processes then are a matter of how various phenomena are interpreted, understood and manifested by single actors and collectivities of actors:

- An actor's interpretation of a phenomenon among available interpretative options
- naming the phenomenon together with the terminology and language used
- other manifestations of the phenomenon
- accepting interpretation and its manifestations (and thereby increasing the legitimacy of the ‘institution’) by an increasing number of actors.

Changes in a Green direction are partly driven by public debate together with EU (or national) environmental and development policy and it is interesting to note that there are cultural differences between countries. In Northern Europe, the popularity of Environmental Management Systems among business leaders is higher than in North America. EMS is now gaining acceptance also in public administration.⁵

Returning now to our Political-Economic-Person-assumptions, it should be observed that the initiatives by individuals are essential for changes in an organization to occur. My own university, Mälardalen, became certified in 1999 as one of the first in Europe and essentially as the result of the work of one dedicated person, Christina von Oelreich. Her ideas were eventually accepted by the rector at the time and now in 2007, the sustainability profile in research and education of the university is more or less accepted. An ecological economics undergraduate program started in 1995, suggesting that some preparations have been going on. But a lot remains to be done, of course.

Concluding comments

The kind of institutional ecological economics presented here is but one of the many alternatives to neoclassical economics. At an early stage of my career, I learnt about institutional economics in the spirit of Thorstein Veblen (Ayres 1964) and I have been part of the Association for Evolutionary Economics (AfEE) and also for some time the European Association for Evolutionary Political Economy. Among more recent institutional economists focusing on environment and development, K. William Kapp (1971, 1976) and Gunnar Myrdal (1978, 1975) have influenced me a lot. Later I have been part of the International Society for Ecological Economics (ISEE) with the journal *Ecological Economics* and the more radical European Society (ESEE).

There are many other schools of thought and associations working for pluralism in economics. This diversity is not unexpected if one accepts the political and ideological nature of any perspective in economics. While some of us see environmental issues as being too low on the political agendas, others look primarily for a social or feminist economics where poverty or gender is the starting point. Hopefully the different associations have something in

⁵ Some scholars and other actors question this incorporation of EMS into public administration. Public administration is and should be, they argue, different from business corporations. As part of a dynamic idea of institutional change processes in multiple steps, EMS can be defended even in universities and public agencies.

common and that it will be possible to refer to some main alternatives to the neoclassical perspective.

In my understanding economics is always political economics in the sense that values and ideologies are always present. As has been argued, the dialogue has to be broadened to include theory of science, ideology and institutional arrangements. I hope this view will be shared by many who thereby will accept that in a democracy no group of scholars can claim monopoly based on one single economics perspective.

How can we then move from monopoly for neoclassical economics at so many departments of economics to pluralism and 'paradigm co-existence'? Since neoclassical economists in my own country largely avoid listening to economists with heterodox views, the main strategy must be one of influencing politicians and other actors through public debate.⁶ Initiatives such as the *Heterodox Economics Newsletter* and the *Post-Autistic Economics Review* are extremely important just as are articles and books (e.g. Fullbrook 2003, 2004). Textbooks pointing to alternative perspectives are very much needed. Politicians as well as students should be "free to choose" also among competing paradigms.

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⁶ Sweden is the country where the Bank of Sweden's Award in Memory of Alfred Nobel is hosted. Although it is possible to identify one or other relatively open-minded person who have received the price, this institution is essentially part of neoclassical protectionism as I have argued in an article in *Dagens Nyheter* (2004b).

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Why is economics not yet a pluralistic science?

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Introduction: the nature of pluralism

Pluralism as a vision of professional interaction in research and pedagogy has acquired a growing following in economics, first and foremost among heterodox economists but also now also among mainstream economists associated with the new research approaches in the field. At the same time, debate and discussion about the nature of pluralism in economics still seems to be at an early stage with many important questions still unaddressed. One major issue concerns the relationship between pluralism seen as a prescription for economic practice and pluralism seen as a description of economic practice. Consider the following two questions. Do calls for pluralism reflect there already being real movement toward pluralism in the discipline? Or, do calls for pluralism help create a basis for pluralism in the discipline? Though many might reject the either/or nature of these questions, and wish to affirm both, the relative weight they place on each proposition makes a difference to how we understand pluralism. That is, if there is a real movement toward pluralism in economics, this would tell us specific things about how pluralism can be supported. Alternatively, if calls for pluralism are primarily instrumental in creating the basis on which pluralism may develop in the discipline, this tells us something else about how pluralism can be supported.

Freeman and Kliman (2006) appear to take the latter view of the matter, namely, they see prescription in the lead, see very little actual pluralism in economics (including in heterodox economics), and hope that a clear and commanding call for pluralism will create a particular kind of pluralism they label 'critical pluralism.' My view is somewhat the opposite of theirs, and is at once both optimistic and pessimistic. I am optimistic in believing that there is an increasing practice of pluralism in economics (in both heterodox and, contrary to what many hold, also in mainstream economics), and that this practice is influencing the culture of economics. I am pessimistic in believing that the limitations that apply to the current practice of pluralism in economics narrow what may realistically be sought in attempts to create a stronger culture of pluralism in economics.

In this paper I seek to contrast these two visions of pluralism in economics, and emphasize the central importance of strategy regarding pluralism in economics. Strategy on this subject depends in my view on sorting out the relationship between pluralism's status as a prescription for economic practice and its use as a description of economic practice. My general view, however, irrespective of how people sort out their different understandings of this relationship, is that there has been very little thinking thus far about pluralism as a 'strategic pluralism,' where this involves determining what goals to pursue relative to the context in which they are pursued (see Davis and Sent, 2006).

This short paper is organized as follows. Section 2 of the paper sets out Freeman and Kliman's critical pluralist conception of pluralism. Section 3 examines the assumptions behind critical pluralism, and argues that their view of natural science, on which it rests, is inaccurate. Section 4 examines the strategy for reform of economics that Freeman and Kliman employ, and

argues that this strategy is unlikely to be effective. Section 5 turns to an alternative view of pluralist reform for economics, drawing on the interconnectedness of values and explanations, and characterizes this view as a strategic pluralism. Section 6 considers the prospects for pluralism in economics in the long run.

Critical pluralism

In their recent contribution to the *Post-Autistics Economic Review*, Alan Freeman and Andrew Kliman (2006) argue that economics is not a pluralistic science, and make a strong case that it ought to be if it is to be a genuine science. Their interpretation of pluralism as critical pluralism identifies a set of obligations they believe all researchers should always observe. Briefly, researchers should critically engage alternative explanations, including their presuppositions, identify the evidence for their own explanations, and identify the evidence for alternative explanations. In a word, critical pluralism is about engagement. Most economists, they argue, pursue their research without consideration of the research and arguments of others. Freeman and Kliman believe, however, that genuinely scientific research is always carried out in the spirit of serious attention to alternative research pathways.

Behind their proposal lies a critique of a strategy for pluralism they attribute to heterodoxy: “we argue that heterodox economists have made the mistake of reducing pluralism to diversity,” where what they mean by this is advocating that there be a multitude of diverse approaches in economics. The problem with this strategy, they believe, is that it results in a set of “monotheoretic” practices largely closed off to one another in a supposed evolutionary “market for economic theory” (31). Proponents of each approach expect their particular approach will ultimately be seen to be true, and accordingly feel little need to engage other approaches. The International Confederation of Associations for Pluralism in Economics (ICAPE) is taken to be an embodiment of this conception of pluralism in that ICAPE is seen as an umbrella organization for heterodox groups that share an antipathy to neoclassicism but otherwise communicate very little with one another. Accordingly, when it comes to heterodoxy’s stance toward orthodoxy, this kind of pluralism is then confined to insisting that every ‘school,’ orthodox or heterodox, be fairly represented within economics as a legitimate school – that is, that economics be re-made in the image of ICAPE. In their view, however, this understanding of pluralism reproduces both between schools and indeed within schools the same intolerance that orthodoxy exhibits vis-à-vis heterodoxy, and thus it can never contribute to the reform of economics as a whole. As an understanding of pluralism, they argue, it goes wrong in failing to appreciate the multiplicity of views within any particular school, the opportunities for real exchange between researchers who disagree, and is contrary to the spirit of engagement they believe characterizes genuine science.

Freeman and Kliman’s answer, then, to the question, why is economics not yet a pluralistic science, is simply that economics is not yet a science. “Our central thesis is that pluralism is not the condiment but the main course. *Because economics is not pluralist, it is not scientific*” (38; original emphasis). Their answer thus resonates with Thorstein Veblen’s and Alfred Eichner’s almost identical answers to similar questions. Veblen asked why economics was not an evolutionary science (Veblen, 1898), and Eichner asked why economics was not yet a science (Eichner, 1983). They both faulted neoclassical economics, because they believed neoclassical economics to be fundamentally nonscientific. For both, neoclassicism constitutes a

metaphysical system not grounded in empirical practices and a culture of open exchange between scientists that permit the development of ideas and theories. Thus like Freeman and Kliman, they regard the main problem as a bad science culture of economics.

Where Veblen and Eichner, on the one hand, and Freeman and Kliman, on the other, seem to disagree, however, is with respect to the confidence we can place on evolutionary forces to create an open science culture in economics. Veblen and Eichner arguably see good epistemological and empirical practice as a positive selection device in economics and social science, whereas Freeman and Kliman argue that “the evolution of ideas in economics selects not for truth, but for political acceptance, above all by those classes in society who fund it” (Freeman and Kliman, 2006, 39). Neoclassicism, then, is selected *for* on Freeman and Kliman’s argument on the grounds of its political acceptability. Alternatively, pluralism in economics is not produced by evolutionary forces. At the same time, the opposite is said to be the case with respect to natural science:

The selection process in the natural sciences is, possibly against the will of the natural scientists, *intrinsically pluralistic*. What we mean by this is that the sciences are organised in such a way that, in the course of their quest to explain natural phenomena, observed reality is tested against *a wide range of possible theoretical explanations* of that reality (*Ibid.*, 42; original emphasis).

In economics, where this does not apply, the ability of a theory to predict is consequently not regarded as an important criterion of acceptance or rejection, with the result that ‘logical coherence’ – too often something merely in the eyes of the beholder – is advanced in the place of empirical adequacy.

Freeman and Kliman’s view of pluralism as critical pluralism is thus a reflection of their understanding of natural science’s scientific culture, and their main recommendation is that economics adopt this culture. They set out this model in terms of seven norms and rules for pluralistic scholarly engagement generated by the International Working Group on Value Theory (IWGVT), and apply it to recent debates over Marx’s value theory. As they emphasize, the

first function of debate is not to settle differences, but, by means of engagement to understand what each alternative is trying to say in its own right, to draw out the implications, and thus see where the differences lie without any prior judgement on which theory or interpretation is necessarily true. At *this* point, when the differences are clear, criteria for deciding between the alternatives can be applied (*Ibid.*, 49-50; original emphasis).

The key criterion, they then add, is empirical success: “The criterion of success for a natural science is empirical. It is that of *prediction*” (41).

A closer look at natural science

There are a number of debatable assumptions underlying Freeman and Kliman's implicit understanding of natural science that deserve examination, but I will only list four of them here which seems particularly contentious:

- (i) natural science is generally pursued in a spirit of open engagement
- (ii) natural science relies on empirical success to determine acceptable theory
- (iii) value judgments and ideology do not limit natural science development
- (iv) critical engagement precedes identifying criteria for judging alternatives

I don't want to suggest that natural science does not have any advantages over social science in these four respects, but rather that the differences between natural science and social science are not as great as Freeman and Kliman imply. This, at the very least, is the message of Thomas Kuhn and much of the subsequent constructivist history of science studies literature (e.g., Barnes, Bloor, and Henry, 1996; Golinksi, 1998). Let me identify what I regard to be two important conclusions of this literature which are at odds with these assumptions. First, empirical testing is often not a determinant of which theories are accepted, and the role it plays in natural science is often framed by the very theories it is meant to test. Second, natural science practice is also quite strongly associated with 'schools' which reflect both the tendency of certain institutions and research locations to favor certain theories and approaches, as well as rely on a variety of 'deep' assumptions scientists hold about reality.

We might ask, then, what motivates the particular view Freeman and Kliman have of the difference between natural science and social science. It is not, they tell us, that natural scientists are better scientists: "Left to their own devices, it is perfectly possible that natural scientists would conduct themselves little differently from the economists" (41). Rather, they believe that natural science has a different social function in a capitalist economy:

a capitalist economy, in which successful competition of capitals demands the successful implementation of technology, imposes a powerful objective constraint [on natural science] Scientific theories are desired by capitalist society because they give rise to products and processes, and these are required to work. This severely limits the selection of bad ideas: theories that lead to bridges or buildings falling down, or aeroplanes falling from the skies, have a limited shelf life" (*Ibid.*).

But how limited a shelf life? This argument assumes a competitive model of capitalism, and rules out monopoly capitalism, path dependency, Microsoft, and a host of questionable technological developments that characterize modern economies which arguably allow shelf lives of technologies to be relatively protracted despite better technologies being possible and often available. Of course, the view that the competitive model applies to capitalism is controversial in economics, including within Marxist economics. Further, while it may well often appear that existing technologies seem reliable, we really don't know what the standard for reliability is since it depends on a host of counterfactual possibilities. Had modern production been organized differently, might existing technologies have been even better?

For example, while it is true that buildings usually don't fall down, we now know that their technologies are not particularly advanced from an environmental perspective, though knowledge of what is needed to make them so has long been available (and is in many cases energy cost-saving as well). Might capitalist production, then, not actually have exerted the pressure on technological development and natural science that Freeman and Kliman assume, and thus only enforced a modest engagement on the part of natural scientists sufficient? Might there even be widespread suppression of technologies that are superior but which would undermine technologies to which monopoly firms are committed?

The risk in Freeman and Kliman's position is that it easily lends itself to simply assuming that natural science is superior to social science in regard to openness and engagement. But the larger issue here concerns what modeling social science on natural science implies about how we think about pluralism and strategies for pluralism in economics. Returning, then, to the issue of pluralism as a prescription for and a description of current economics, what is Freeman and Kliman's view of the relationship between pluralism as a prescription and as a description, and what does this imply about strategies for pluralism?

The strategy of critical pluralism

Recall that Freeman and Kliman see very little actual pluralism in economics – thus their view that we need to reach outside of economics to natural science to create a culture of pluralism for economics. This then entails their view of the relationship between pluralism as a prescription and as a description, namely, that prescription needs to take the lead to create a basis on which pluralism may develop in the discipline. Specifically, that basis is critical pluralism understood as critical engagement between researchers. Broadly, then, their strategy for pluralism is a matter of embedding this ideal in the practices and culture of economics. How might this strategy be pursued?

On the surface of things, it would seem that they have already made the case that there is *no* way to pursue such a strategy. Indeed Freeman and Kliman not only say there is very little actual pluralism in economics, but also say that economics is incapable of reforming itself. Yet they do see one hope for reforming economics.

We believe economics is ... incapable of self-reform. Our reform programme is therefore not primarily addressed to economists but to the consumers of their product (32).

In our view ... the fault in economics lies in the entire notion that the job of the economist is to judge, on behalf of the consumers of economics, what is a correct theory. We sustain that the function of economic research is, on the contrary, to lay bare the concealed assumptions behind theories so that the consumers of our output may for themselves judge between them (34).

In effect, then, they substitute for the effect they believe that the competition of capitals has on technology development in natural science an effect they believe the various consumers of economics could have on the development of economics.

But why should we expect the consumers of economics to be in any position to impose significant pressures on economists? One important thing about the argument concerning technology and the competition between capitals is that it identifies a unified force which in principle affects the behavior of all natural scientists in the same way. New technologies, as well as responses to them, need to be genuinely innovative. Research that is ideological should be unaffordable. But by comparison, the consumers of economics are a variety of different interest groups, who accordingly exert a variety of different types of pressure on economists. For example, public policy based on the standard theory of labor markets has at least two major constituencies whose respective goals for the functioning of labor markets are in many ways opposed. One constituency may regard the enactment of a particular policy as a success which the other regards as a failure (for example, a minimum wage law). *Prima facie*, then, it is not true that “consumers of our output may for themselves judge between them,” but rather that economists have considerable freedom to advance those ideological positions that are best suited to the different interests among consumers they wish to serve, exactly as Freeman and Kliman say has historically been the case. Indeed why should the future be any different from the past?

Thus, just as it seems unrealistic to reach outside of economics to natural science to introduce pluralist ideals, so it seems unrealistic to reach outside of economics to the consumers of economics to apply a pressure for pluralism in economics. I suggest, then, that the problem with treating pluralism primarily as a prescription meant to lay basis for pluralism in practice is that the perceived absence of a basis for pluralism in economics gives these external points of influence no detectable leverage on economics. Essentially what Freeman and Kliman consequently offer is an abstract ethical idea, despite their denial that this is the upshot of their position.

It may be thought that such a programme is normative and ethical, rather than positive or scientific. We will argue that, on the contrary, without formal guarantees of pluralism and critical method, economics does not function as a science. Our guiding principle is to identify those practices which society must impose on its economists, should it require these economists to provide them scientifically valid information (32).

But the logic here seems circular. Economics, they seem to be saying, will not become a science until it becomes a science, and this can only occur by having pluralist practices imposed upon it. Thus Freeman and Kliman’s strategy, it appears, is *only* normative and ethical. Given, then, the unlikelihood that consumers of economics can impose this ideal on economics, the implication seems to be that a strategy of pluralism needs to be normative and ethical while *also* being based on real movement toward pluralism already in economics. That basis may be admittedly inadequate in important respects. Freeman and Kliman are certainly perceptive in their judgment of a pluralism of diversity and schools as tending to incorporate the same intolerances orthodoxy exhibits toward heterodoxy. They are also surely correct in emphasizing the need to set high standards for pluralism, and who would dispute the integrity of their vision of pluralism as critical engagement? My complaint, rather, is one that concerns the best strategy for pluralism, and accordingly in the following section I turn to the idea of a strategic pluralism.

Strategic Pluralism

Strategic pluralism begins with the idea that calls for pluralism must target existing commitments to pluralism in economics. From a social economic perspective, values and explanations are indissolubly linked, and thus prescriptions and descriptions are always tied to one another. The strategic part of this idea lies in working out the specific connections between them, and doing so in a way that preserves both. Thus, if a certain descriptive basis for pluralistic practice exists in economics, prescriptive calls for pluralism begin on that basis, but must also go beyond it – otherwise they offer nothing normative. The business of how one goes beyond current practice, or how particular standards for pluralism may be effective in influencing current practice, is of course subject to different opinions about the best strategy possible. I will offer one view of such a strategy, and then apply it to the current situation in economics.

First, however, to demonstrate the kinds of constraints that current pluralist practice, such as it is, imposes on prescriptions for pluralism, let me set out a type of strategy which is arguably *not* effective as a means of developing pluralist practice in economics, even though it still involves what I consider a strategic pluralism. This might be termed a strategy of demonstrating contradictions between current practices and the pluralist ideals associated with those same practices as operate in particular schools or approaches in economics. The strategy might proceed as follows: identify a current pluralist practice in economics within a school or approach; describe inconsistencies in this practice vis-à-vis other schools or approaches; then argue in the name of pluralism that these inconsistencies should be eliminated, thus extending pluralist practice and further enhancing the ideal of pluralism in that school or approach (as well in economics as a whole). For example, consider recent behavioral economics and its critiques of neoclassical rational choice theory. As the economics profession has long resisted critiques of the theory of choice, behavioral economists have argued that the field should be more open and embrace a variety of approaches to explaining choice (e.g., Starmer, 2000). At the same time, however, many feminist economists would likely say that behavioral economics still largely ignores the role of gender in choice. This might accordingly be registered as an inconsistency, and then presented to behavioral economists for them to address, accompanied by a call for a more pluralistic behavioral economics, on the grounds that such a development is consistent with behavioral economics' existing basis for pluralism.

The problem with this strategy in my view is due to the constraints imposed by economics' pluralist division into schools or approaches. The feminist critique arises outside of the behavioralist school, and operates by showing an inconsistency *across* schools. But on the argument Freeman and Kliman advance regarding the nature of current economics with its associated intolerance between schools, this critique is likely to be dismissed out of hand by behavioral economists, despite its being a valid critique from their own perspective, and despite its being an extension of their pluralist critique of neoclassical intolerance, solely for the reason that it originates in another school.

Though Freeman and Kliman do not consider the existence of competing schools in economics a basis for pluralism, it seems to be more accurate to say that the existence of competing schools in economics creates a particular kind of pluralism, since the existence of competing schools produces a form of heterogeneity different and indeed stronger than is involved in there being distinct orientations within a single paradigm. It is this specific kind of

pluralism which gives rise to the diversity ideal, which though obviously modest by their standard of critical pluralism nonetheless involves one kind of pluralist ideal. The point that follows from this, then, is that the modest basis which a 'diversity pluralism' offers has two sides to it. It bars certain kinds of attempts to extend pluralism, particularly those that directly challenge the autonomy of schools, but it also creates specific opportunities for extending pluralism.

The kind of strategic pluralism I recommend, then, aims to operate within the constraint of diversity pluralism but also aims to create possibilities for a broader form of pluralism. Specifically, rather than demonstrating contradictions across schools as an argument for extending pluralism, it seeks to demonstrate shared principles across schools to reduce intolerance between them, and thereby generate greater support for pluralism in general. On Freeman and Kliman's view, schools are "monotheoretic" in their exclusive commitment to their own programs, and the defense of diversity is really just a form of self-defense. But this self-defense can come to be perceived as encompassing the goals of other schools if a school's own principles are seen as shared with other schools. Indeed this argument has been advanced quite explicitly in ICAPE and for heterodoxy in general (Lawson, 2006; Lee, 2006) and separately also for the new approaches in economics (Gintis, 2007). I have argued that it can and ought to be advanced with respect to principles shared by heterodoxy and the new approaches in economics (Davis, 2006). Let me give one example of this argument about shared principles to illustrate.

Behavioral economics rejects the neoclassical atomistic individual conception on the grounds that preferences are believed to be endogenously constructed rather than exogenously given (Camerer and Loewenstein, 2003). Preferences are framed, anchored, elicited, and malleable, depending on the context in which individuals find themselves when they make choices. Individuals are accordingly 'socially embedded' in the sense that their choices depend on the social contexts in which they make them. This conception, however, is very much like the one which operates in many heterodox approaches that argue individuals are social in nature. This is not to say that differences do not exist between the understanding behavioral economics has of individuals' social embeddedness and the general heterodox understanding of it. The behavioral conception treats the concept of 'social' far more abstractly and ahistorically than does the heterodox conception. But both nonetheless reject the neoclassical atomistic individual conception, and this arguably allows bridges to be built between the behavioral and heterodox conceptions.

How, then, ought one to proceed in advancing pluralism by targeting this shared principle? One thing possible is that heterodox economists who are motivated to show that the context of choice incorporates a larger sense of the 'social' than many behavioral economists employ ought to produce explanations of contextualized choice that are institutionally rich, and do so by showing how the behaviorist language of preferences – their being framed, anchored, elicited, and malleable depending on their context – reflects concrete institutional settings. In fact, there is precedent for this wider social-institutional embedding in research already being carried out by behavioral economists, for example on individual choices in pension systems (e.g., Mitchell and Utkus, 2004), and indeed one member associate of ICAPE, the Society for the Advancement of Behavioral Economics (SABE), is active in research emphasizing the wider social-institutional dimensions of contextualized choice.

My argument, then, is that this kind of strategy for advancing pluralism – one kind of strategic pluralism – not only operates within the constraints of an existing diversity pluralism in economics, but also offers the promise of extending pluralist practices in economics by developing links between different schools. It thus builds prescription around description rather than pose norms and standards that have little or no existing basis in the field, and accordingly constitutes what seems a more realistic approach to the problem of pluralism in economics. In the remaining section of this paper, I turn to what pursuing this kind of strategic pluralism might mean to economics in the long run.

Pluralism in the long run

It is always tempting to see the future as a reflection of the past, and so many are no doubt inclined to see the prospects for pluralism in economics as not very promising. The long dominance of economics by neoclassicism gives good grounds for this view, and the vulnerable and marginalized position of heterodox economics – where pluralism is explicitly defended – reinforces it. One might, however, argue that it is becoming increasingly difficult for economics to be dominated by single approaches, and that there will be a steady continuing emergence of new approaches in the field in the future. Basically, so this argument would go, the object of economics, the economy, is only becoming increasingly complex with a growing multitude of dimensions and aspects, so that not only are new approaches to explaining different previously unrecognized aspects of the economy continually arising, but no single approach seems any longer to be sufficiently comprehensive to explain the economy in its diverse dimensions and aspects. Compounding this is the apparent increase in interdisciplinarity across all the sciences. Increased cross-boundary borrowing together with conceptual exports and imports between sciences seems to be the product of an expansion of science in general in the last half century. But such transfers inject materials into sciences that usually do not immediately conform with what is already there, thus further multiplying the heterogeneous character of the sciences.

If these patterns of development characterize the future, then economics would regularly see the emergence of new approaches, many laying the foundations for new schools. Though dominant approaches may still arise, their tenure might be briefer, and their hold on economics as a whole more fragile. What this would then mean in the framework of the discussion here is that diversity pluralism or the pluralism of schools would regularly receive new impetus. Rather than ICAPE being an exceptional development, it might indeed become a general model within economics. This would not necessarily guarantee, however, an increasing tolerance within economics, since as Freeman and Kliman recognize, the existence of schools can be more about boundaries than open exchange. At the same time, a diversity pluralism allows for the possibility of a strategic pluralism that can establish tolerance as a general value in economics, perhaps not by the standard of critical engagement, but something not to be dismissed either.

The distinction between tolerance and critical engagement recalls another important distinction worth noting when we think about things we hope to achieve. Comparing different kinds of societies we may distinguish between those societies whose institutions do not humiliate individuals – what may be termed decent societies – and societies whose individuals do not humiliate other individuals – what may be termed civilized societies (Margalit, 1996). With respect to pluralism, decent societies might be said to exhibit tolerance and offer a kind of

diversity pluralism, whereas civilized societies might be said to exhibit the higher standard of critical pluralism. Needless to say, the conditions required to achieve the latter are more demanding. We all, moreover, presumably hope to live in a world of the latter, but if that is not possible, it would still be an achievement to live in a world of the former.

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Grounding the conversation to ensure a better textbook

A comment on: "Is There Life after Samuelson's Economics? Changing the Textbooks", *post-autistic economics review*, issue no. 42, 18 May 2007, pp. 2-7.

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Klamer, McCloskey and Ziliak promise a new economics textbook, *The Economic Conversation*, to help displace the Samuelson knockoffs that so impede post-autistic courses in introductory economics. The authors have courageously invited criticisms and contributions to their work-in-progress through a website.²

In *The Economic Conversation*, the authors use dialogue as a means to "show economics... to be a controversial and conversational subject, thoroughly 'rhetorical' ... where people start in disagreement with one another, and seek to persuade more or less reasonably to an end of at least mutual understanding." Yet while humans can and do disagree over the best way to understand, to analyze, to shape and to evaluate the performance of the economy, rhetoric and disagreements do not allow humanity to escape biophysical constraints. The draft text by Klamer, McCloskey and Ziliak, like its Samuelsonian counterparts, currently conceptualizes the economy as existing independently of the biosphere.³ Unless students seek to understand the limitations of the text, they risk being handicapped in trying to make wise and informed choices on critical matters of public policy when they take on positions of power and influence.⁴

To be relevant and useful to students, textbooks need to address the world that students will be facing. *The Economic Conversation* is coming out in 2008, not 1948. Students are coming of age in a world with alarming ecological trends that suggest ever more challenging conditions for achieving human wellbeing and economic security. For instance, the level of carbon dioxide in the atmosphere has climbed from pre-industrial levels of 280 ppm to 379 ppm in 2005. It is now higher than at any time in the past 650,000 years, and is climbing at 1.9 ppm per year. Under business as usual, there is a 50% risk of average global temperatures climbing by 5°C in coming decades, taking humanity into unknown territory and catastrophic change.⁵ Stern's recent report

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² www.theeconomicconversation.com. My review of their material is based on what was available on their website as of May 25, 2007.

³ For a recent critique see: Reardon, Jack 2007. "How green are principles texts? An investigation into how mainstream economics educates students pertaining to energy, the environment and green economics", *International Journal of Green Economics*. 1(3/4):381-393.

⁴ While 40% of American students are exposed to an undergraduate economics course, only about 2% major in economics. Siegfried, J. J. (2000) 'How many college students are exposed to economics?' *Journal of Economic Education*, vol. 31, pp. 202-4. So for a large proportion of the student population, the introductory economics course is likely to be very influential on their subsequent economic thinking.

to the UK government noted that climate change “presents a unique challenge for economics: it is the greatest and widest-ranging market failure ever seen.”⁶

While the whole text is not yet available for review, material on the authors’ website shows that at least from an ecosystem-economy linkages perspective⁷, there are indications that the text will not live up to its “post-autistic” billing.

In *The Economic Conversation*’s concluding section, the authors sum up the key take home lessons for students:

“If you remember only one picture from this book, make it the circular flow. Everything, as Bob Marley sings in a song, “goes around and comes around.” What shows up as production on one side of the economy also shows up as income on the other side. Expenditure equals income. Gross Domestic Product equals total national income (ignoring a few *The Economic Conversation*’s adjustments). What goes around comes around, as shown by the circular flow.”⁸

The circular flow has an honoured place in introductory economics textbooks and *The Economic Conversation* promises to be no different, as the authors promote their use of the diagram as a unifying analytical device.^{9,10} The circular flow conceptualizes the economy as existing in isolation from the environment, omitting the natural resources the economy consumes, the fossil energy that powers it, the extensive area of habitat it takes over or degrades, and the wastes it creates. The circular flow diagram thereby teaches students to believe economies are perpetual motion machines.

⁵ See Intergovernmental Panel on Climate Change, Working Group 1: The physical basis of climate change’s fourth assessment report (2006) at: <http://ipcc-wg1.ucar.edu/wg1/wg1-report.html> (accessed May 26, 2007) and Stern, Nicholas. 2006. *The Economics of Climate Change: The Stern Review*. Cabinet Office - HM Treasury. London. There may be even less time for humanity to act to forestall disaster, if global warming causes feedback effects such as the rapid conversion of the Amazon rainforest into a savannah, with the large store of carbon released through fires pushing the climate out of control. Amazon rainforest ‘could become a desert’, *The Independent*, July 23, 2006.

⁶ Stern, 2006.

⁷ I concur with the arguments of Costanza, Daly and others that if economics is to be post-autistic, it needs to address insights from ecological economics. See for instance, Robert Costanza, “Ecological Economics is Post-Autistic”, *post-autistic economics review*, issue no. 20, 3 June 2003, article 2, <http://www.paecon.net/PAERReview/issue20/Costanza20.htm>

⁸ *The Economic Conversation*, Chapter 34 preview: <http://www.theeconomicconversation.com/book/ch34.2.php>.

⁹ *The Economic Conversation*, Preface to teachers, <http://www.theeconomicconversation.com/teachers.php>.

¹⁰ See Daly, H. E. 1991. “Towards an Environmental Macroeconomics”, *Land Economics*, Vol. 67, No. 2, pp. 255-259 and Ehrlich, P. R. 1989. “The limits to substitution: Meta-Resource depletion and a new economic-ecological approach.” *Ecological Economics* (1) 9-16.

Contrast the above with the treatment of the circular flow diagram in a recent, post-autistic textbook, *Microeconomics in Context*:

...the circular flow diagram is a little like a “perpetual motion machine”; the economy it portrays can apparently keep on generating products forever without any inputs of materials or energy. The necessity of resource maintenance activities is ignored....¹¹

How well will the textbook help students understand and anticipate ecological threats and declining flows of natural resources and ecosystem services? ¹² A search of the material now available on *The Economic Conversation* website is less than encouraging. Searches for the terms “ecosystem services,” “atmosphere,” “fish,” “soil,” “trees,” “forest,” “biodiversity,” “ecological limits,” “limits to growth,” “ecology,” “thermodynamics” come up empty.¹³ “Global warming” merits a mention as one of the issues to which economics can bring insights. “Ecological” brings up a discussion on how property rights can affect the resulting “ecological balance” under cattle grazing. Searches for the terms “pollution” and “externalities” do a little better, with almost a dozen hits each; these references involve narrow expositions of externalities, optimality, property rights and the first and second Coase theorems. Searching for “oil” produces some hits, but none that I could find that hinted of the problems humanity faces with peak oil and a carbon constrained future; “non-renewable resources” and “fossil fuels” come up empty.¹⁴ The word “environmental” comes up in the preface, where the authors suggest that in working at places like the “Environmental Defense Fund,” students will need to be able to persuade other people. In a discussion on growth, the text concedes:

...not everyone likes what comes with economic growth. A new highway means a loss of unspoiled countryside, or a stressful drive in the car instead of a leisurely walk to the old neighbourhood grocery store. A bigger city means more traffic congestion. Increased production means more air pollution. Some people take the view... that economic growth means a bad trade-off between quality of life and quantity produced.¹⁵

¹¹ Goodwin, N., Nelson, J., Ackerman, F and Weisskopf, T. 2005. *Microeconomics in context*. Boston: Houghton Mifflin Company. Page 44.

¹² See my comparison in the popular press of two textbooks that do address the ecological fundamentals against the Samuelson genre. Green, Tom 2006. “The revolution will begin with a textbook”, *Adbusters* vol. 69.

¹³ Sixteen years earlier, Daly (1991) reported that he found no entries in the indexes of three leading macroeconomic textbooks for the terms “natural resources”, “environment”, “depletion” and “pollution.”

¹⁴ Relying on unconventional oil and coal in a carbon constrained world and alternative fuels all present their own challenges and ecological impacts. As the Danish Board of The Economic Conversationhology concluded, “History may reveal that the prevailing axiom of sustainable economic growth is a theoretical derivative of cheap-oil.” Danish Board of The Economic Conversationhology and the Society of Danish Engineers, 2004. *Oil-based The Economic Conversationhology and Economy Prospects for the Future*. Available at: http://www.tekno.dk/pdf/projekter/p04_Oil-based_The_Economic_Conversationhology_and_Economy.pdf (accessed May 26, 2007). Even optimistic assumptions show a need for urgent transition to alternative energy sources. See: Greene, David, Hopson, Janet and Li, Jia 2006. “Have we run out of oil yet? Oil peaking analysis from an optimist's perspective.” *Energy Policy* 34 (5): 515-531.

Their characterization of the growth-environment nexus is limited to an environment-as-amenity perspective and focuses on how growth can impinge quality of life¹⁶. They ignore how worsening ecological and resource trends are related to exponential growth in the scale of the economy relative to the encompassing ecosystem: from collapsing fish stocks¹⁷ to loss of forest cover¹⁸, humanity is living beyond its ecological means and is degrading the very ecosystems on which its wellbeing depends.^{19, 20} In a passage that could be lifted from a mainstream text, students are left with no doubt as to the officially sanctioned belief: “essentially every economist agrees that the macroeconomic promised land has ... a high rate of economic growth per capita.”²¹

In one of the dialogues, McCloskey argues “It’s good that we [economists] are around to point out that cleaning up the environment has costs which, if considered well, may not always be worth the cleanliness.”²² Using a “cleanliness” lens shows a lack of sophistication. Most environmental issues, such as overfishing, biodiversity loss, the invasion of exotic species, or habitat fragmentation, can be characterized as an issue of “cleanliness” or “cleaning up the environment.” Cleanliness focuses us on litter, on the condition of the local park: it is the view of the environment as an amenity, rather than something we are ultimately dependent upon. Also, given current ecological crises, why does McCloskey focus on the cost of overacting? If the last

¹⁵ From chapter 20, Section 7 – Issues in Macroeconomics: Economic Growth and Development.

¹⁶ Even from the narrow quality of life / amenity standpoint, the desirability of growth is questionable since with more growth industrialized countries are achieving declining (if not negative) marginal benefits, and increasing marginal costs. But much more important is the danger that further growth accelerates degradation of the planet’s capacity to supply desired resources, ecosystem services and viable living conditions. The authors later they mention Herman Daly as an economist concerned about growth and the field of “ecological macroeconomics.” It is curious that they don’t refer to ecological economics in their text, or in their website invitation to “Frustrated neoclassicals, feminists and libertarians, empirical Marxists and post-modern Keynesians, and everyone in between” to comment on their text. While it was not the focus of my review nor my area of expertise, it seems to me that *The Economic Conversation* could better address issues raised in feminist economics.

¹⁷ Worm, B., Barbier, E., Beaumont, J. et al., 2006 “Impacts of Biodiversity Loss on Ocean Ecosystem Services” *Science* 314 (3 November 2006).

¹⁸ Food and Agriculture Organization (FAO) (2007). *State of the World’s Forests*.

¹⁹ United Nations Environment Program (UNEP) (2005). *Living Beyond Our Means: Natural Assets and Human Well-Being*. Statement of the Millennium Ecosystem Assessment Board. UNEP.

²⁰ Rees, W. 2002. “An Ecological Economics Perspective on Sustainability and Prospects for Ending Poverty,” *Population and Environment* 24(1): 15-46.

²¹ *The Economic Conversation* chapter 20, section “Six Macroeconomic Goals of the Promised Land.” This reference to the promised land reminds me of Galbraith’s comment: “Saint Peter is assumed to ask applicants only what they have done to increase GDP,” Galbraith, John K. 2007 [1967]. *The New Industrial State*. Princeton University Press. Page 497.

²² *The Economic Conversation*, Chapter 34.

half-century is any indication, and due in no small part to the contribution of mainstream economics, there is little risk that humanity will act too aggressively to improve ecological prospects.

While the authors' intentions are commendable, students studying economics circa 2008 deserve conversations grounded in biophysical reality and in the ecological predicaments of our era. One would expect that a new economics textbook that promised to be post-autistic would address the relationship between the economy and the environment at the foundational level, rather than continuing to add the environment in as an afterthought through the limiting lens of externalities.²³ Hopefully my critique will not apply to the final product.

²³ Herman Daly has written, "...which we classify as 'external' costs for no better reason than because we have made no provision for them in our economic theories." Daly, H.E., 1992. *Steady State Economics: Second Edition with New Essays*. Earthscan, page 88. While an externalities approach may have once been a sufficient approximation due to the relatively small economy of times past, the global economy has grown by a factor of 40 since 1820, while the Earth's dimensions have been rather stable.

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French elections: start of a new phase

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The French elections were a 'first' in modern history in one respect that has not been acknowledged or perhaps even noticed. It is the first time the candidates have taken overtly different positions on how their country should handle its response to the global competitive market. Normally, both contending parties take as given that the global market is 'a fact of life', and each claims they will do a better job of making their economy more competitive to cope with it.

In other words, it is the first recent occasion that an electorate has been presented with a real choice. Sarkozy offered, in effect, structural adjustment of the economy. That means reduced social services; and changes in employment law – fewer restrictions on wages and conditions of work, easier terms of hiring and firing, longer working hours – in order to lower labour costs, make enterprise cheaper and more competitive, increase exports and attract capital. Sarkozy was presented as modern, realistic, the father of a new French renaissance.

Royal offered, in effect, a programme to protect employment standards and promote a more national economy, which would substitute French production for imports. We know little about the details of Royal's programme, because it was reported in the mainstream media, if at all, as kind of wacky: old-fashioned feather-bedding of workers, a nightmare for employers, so a recipe for decline in France.

One result of being presented with real alternatives was an 85% turnout at the polls. Contrast that with a secular downward trend in voter turnout for two decades in Europe and America. And the difference between the votes for the two parties was only some 3%. Of the 85% that voted, just under half voted against the father of the new French renaissance.

This offer of real alternatives - rather than apparent bickering between people offering much the same – is what brought out the voters. Blair's economics is much the same as Cameron's; so are those of Bush and Clinton; the ANC and the DA; the rival German parties, as well as the Italians. And so on. This is not to say there are no dividing issues: Iraq is clearly one, and so are various ethnic rivalries.

But the political *economy* was, until modern times, the stuff of political debate. Clinton's '*It's the economy, stupid*' did not mean, sadly, that his economic policies were very different from those of his Republican rivals – only that his party was running it better. Royal and Sarkozy showed that there are two opposing approaches within the free market system.

'*The people of France have chosen change*', Sarkozy said. He is mistaken. Just under half of the people (those who voted for him) have chosen more of the same - only more punitive for those of their number who work for wages and salaries.

He is quite right that short of a change in the rules of the global market, every country in Europe – perhaps first, but not only, the French – will have to adjust their standards of living to

compete with the new industrial giants of the East. Already there are areas in Europe and the US that constitute deserts, bereft of economic activity, undercut by the Chinese and others' prices. This is noted in mainstream economics as a necessary adjustment before new and modern activity springs up.

Occasionally, it does, helped by government subsidy. But on the whole, nothing springs up in those areas: they become broken, derelict, vandalised, burglar-barred remnants of shops and miserable roofs for homeless people and addicted wrecks.

Royal said: '*Something has risen up that will not stop.*' I reckon she is right. Her vote – indeed her very platform – is a sign of a political trend that 'will not stop'. At the time of the referenda for the EU constitution, there were actual riots in France – and elsewhere. They were interpreted as race-based and/or signifying typical French xenophobia. They were in fact a rejection of an economic system that ruthlessly and relentlessly makes working people pay the full price for a country's economic success. Voters rejected the EU constitution because they saw it as representing the current global dispensation.

What is happening is that ordinary European, and American, voters are beginning to make common cause with the victims of that dispensation in poor countries. First world workers are not starving or deprived of water and electricity because of recent privatisation; but they are poorer than they were, their work is more casualised, their incomes less predictable and their access to education and other services now disputed. They do not have to be doctrinaire politicians or Marxist fundamentals to realise they do not like it.

Royal, it seems, tapped into that. She didn't win, but very nearly. She will certainly not be the last to take that direction.

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Economic freedom for the rest of us

Jim Stanford [Canadian Auto Workers]

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Thank you for Margaret Legum's solid critique of the Economic Freedom Index¹ -- a silly project that is sponsored by several right-wing think tanks around the world (including the Heritage Foundation in the U.S., and Canada's Fraser Institute which actually started the whole thing).

The thinking behind the Index is thoroughly neoclassical: markets work best when government intervention is minimized, and private sector agents are given maximum "freedom" to produce and accumulate. The variables which enter this index (many of which are subjective scores, rather than empirical data) reflect this orientation. A country is free if it has low taxes, weak regulation (including labour market regulation), and free trade. One form of government intervention which is desirable, of course, is the active protection of property rights (including increasingly abstract intellectual property rights); this variable enters the Index with a positive weighting.

The obvious question to be asked, however, is: "Freedom for who?" The choice of variables in the right-wing freedom index assumes that what is good for investors and employers, is good for everyone (trickle-down writ large). In reality, however, economic freedom is in the eye of the beholder. What enhances freedom for an employer (eg. the freedom to hire labour at the cheapest wage possible) undermines economic freedom for his or her employees (eg. the freedom to work in a job without suffering poverty).

All this is reminiscent, of course, of Anatole France's famous quote: "The law, in its majestic equality, forbids the rich as well as the poor to sleep under bridges, to beg in the streets, and to steal bread."

The Fraser Institute has a Canadian version of the Economic Freedom Index which ranks Canada's ten provinces according to their freedom scores. In conjunction with the Canadian Centre for Policy Alternatives (Canada's main progressive think tank), I prepared two studies earlier this decade which constructed an alternative index. This index was called Economic Freedom for the Rest of Us (or EFRU for short -- the acronym sounds deliberately like F-you!). It was composed of various indices of the extent to which average people (as opposed to employers and investors) are able to support themselves in a reasonably prosperous and secure manner. Some of our variables (such as trade union penetration) also appeared in the Fraser Institute's index ... but with the opposite sign! Needless to say, the ranking of Canada's provinces differed considerably depending on which vision of "freedom" is utilized.

Here are links to the two EFRU studies:

http://policyalternatives.ca/documents/National_Office_Pubs/efru.pdf

http://policyalternatives.ca/documents/National_Office_Pubs/efru2000.pdf

¹ Margaret Legum, "Should We Aspire to a High Score for 'Economic Freedom'?", *post-autistic economics review*, issue no. 42, 18 May 2007, p. 60, <http://www.paecon.net/PAERreview/issue42/Legum42.htm>

I wonder if progressive economists might be interested in networking internationally to produce an alternative global index which similarly attempts to measure economic freedom -- for the rest of us.

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