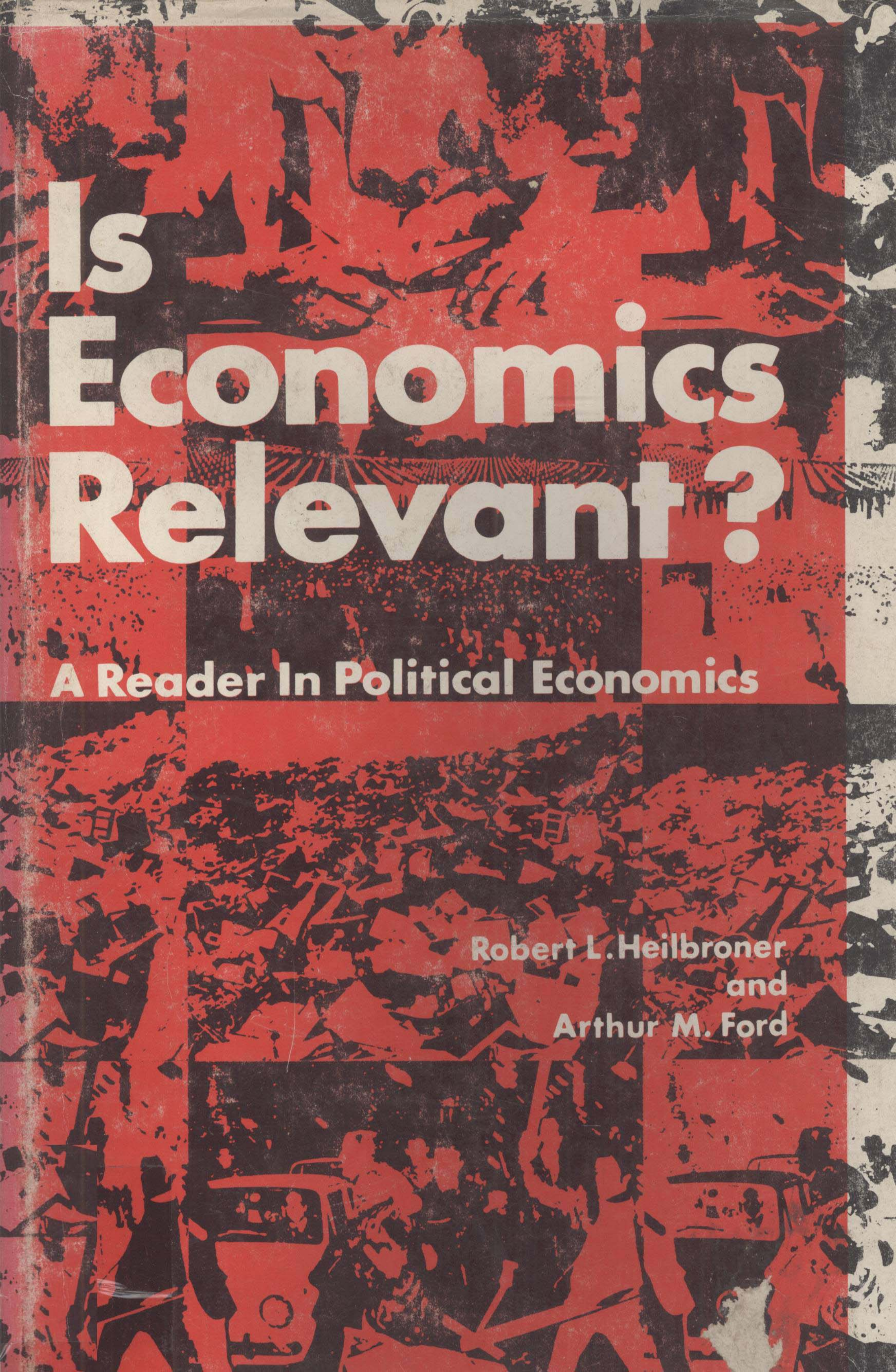

Is Economics Relevant?

A Reader In Political Economics

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and
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IS ECONOMICS RELEVANT?
A Reader In Political Economics

For Joan and Ramona

INTRODUCTION

ROBERT L. HEILBRONER

There is a word that makes professors of economics wince these days, as I can testify from personal experience. The word is, of course, *relevance*. There was a time, not so many years ago, when I could teach an introductory class the mysteries of diminishing marginal utility, explaining why the man in the Sahara desert would not be willing to pay as much for the third pint of water as for the second, confident that when the hands went up it would be because someone wasn't convinced that he shouldn't pay more, because his *total* utility was greater. Now when the hands go up, I know what the question is going to be: "That's clear enough, Professor Heilbroner, but we don't see how it's relevant."

Is it relevant? It is certainly easy enough to understand why it does not seem so. What has diminishing marginal utility to do with giant corporations, the military-industrial complex, imperialism, ghetto life? Isn't time spent on the study of marginal utility simply time diverted from the consideration of real issues, such as these? Worse, isn't the very act of taking seriously a figment like "diminishing marginal utility" apt to cultivate an ivory-tower frame of mind that will no longer wish to come to grips with the brute problems of the real world?

I think these are the kinds of misgivings that first come to the surface when economics students begin to ask questions about the discipline they are learning, rather than merely swallowing it down like so much medicine. Yet I do not think that these initial objections count for very much. As a rule, the aspect of economics that upsets those who begin to study it is its abstractness, its seeming removal from life, but any instructor worth his salt can reassure his students that this abstract quality is a strength and not a weakness if we are to study large-scale questions, and that the "unreality" of many economic conceptions conceals a sharp cutting edge.

Thus, for example, the rationale for progressive taxation hinges on nothing less than the belief that successive dollars of income, like successive pints of water in the Sahara, yield ever smaller increments of enjoyment to its recipients. In the same way, an ivory-tower idea such as pure competition, which every first-year student regards as utterly irrelevant, suddenly turns up as the indispensable starting point for an understanding of Marx's model of capitalism; or the rarified assumptions of Pareto Optimality (that imaginary condition in which no further efficiency or consumer satisfaction can be squeezed out of a given economic system by rearranging its inputs or outputs) take on an unexpected political and social relevance in discussing the problems of socialist planning.

Indeed, by the time an overly zealous instructor is through, the danger is that the shoe will be on the other foot, and that the class will have been persuaded that the charge of "irrelevance" is nothing but the ill-considered objections of those who have not yet mastered the subject. But if he proceeds this far, it is now the instructor who risks becoming irrelevant. For if the initial objections to the abstractions of economics tend to be wide of the mark, this is very far from saying that the feelings of unease aroused by the study of economics have no validity. What the freshman student wants from economics—and hopefully what he will continue to want when he has become an instructor—is a heightened ability to understand, and if possible to control, important aspects of the social system in which he lives. Long after he has accepted the need for the abstract character of economic thought, the student (and his instructor, too) may still feel that economics ignores the most pressing issues of society, or that it gives unsatisfactory answers to them. At that point, the charge of "irrelevance" is no longer an objection that can be easily overcome, but a serious challenge to the validity of the discipline itself.

Is economics a penetrative and reliable guide to the nature of society? The purpose of this book of readings is to demonstrate that it *can* be—that it can ask piercing questions, give cogent advice, and offer deep perspectives on history and on social evolution. To that extent, of course, economics is as relevant as any study of society can be. But in a sense, a book of readings that emphasizes the relevance of economics fails to explain the other side of the coin—the reasons why economics is often not relevant. It would hardly do to fill the pages of this book with examples of economics at its worst. Hence, in this initial essay I shall try to point out why and to what exent economics does not succeed in being useful; that is, why economics frequently does not ask the kinds of questions that would most clearly illumine society, or why it gets unsatisfactory answers to some of the questions it does ask, or why it often fails to offer us the historic or philosophic guidance we seek from it.

The Irrelevance of Economists

Let me begin this analysis of the failures of economics by taking up a touchy issue, but one that cannot be sidestepped. This is the fact that the "irrelevance" that most disturbs many students is the unwillingness of academic economists to ask disturbing or unpleasant questions with regard to the social order, and in particular to avoid social criticism that is radical in intent. Economics thus appears to many students not as a genuinely objective science that sheds its illumination on the good and bad aspects of society alike, but as a kind of high-level apologetics that tends to illumine only those issues for which economics has an "answer," and to overlook those for which it has none.

I think one should admit that, on the whole, this criticism is fairly taken. Most textbooks are bland in tone and pussyfoot around thorny questions. How many, for example, ever mention the issues of imperialism, or present the facts with regard to the concentration of wealth in the United States, or examine very deeply the behavior of the corporate sector? Moreover, students who have gone beyond the textbooks into the professional journals know that this blandness is by no means confined to the delicate atmosphere of the classroom, but extends into the dialogue that the profession holds with itself. With exceptions to which we will return, it is simply a fact that most of the things that economists write about are not matters of burning social importance, and that the prevailing tone in which they do write about social questions tends to be one of a sympathetic conservatism rather than of indignant radicalism.

Why are most economists so conservative in their outlook? Professor Stigler, one of the best-known exponents of the conservative economic philosophy, has contended that it is the result of the training that economists undergo, a training that disabuses them of heady notions with respect to the changes that socialism (or some other form of institutional rearrangement) could bring and that persuades them of the propriety of the market system.[1]

It is probably true that a study of economics does tend to make one

[1]Stigler's essay, "The Politics of Political Economists" first appeared in the *Quarterly Journal of Economics* (November 1959) and has been reprinted in his *Essays in the History of Economic Thought*. His actual words read: "It becomes impossible for the trained economist to believe that a small group of selfish capitalists dictates the main outlines of the allocation of resources. . . . He cannot unblushingly repeat such slogans as 'production for use rather than for profit.' He cannot believe that a change in the *form* of social organization will eliminate basic economic problems." (*Essays*, pp. 59–60.)

wary of sweeping statements and unconsidered jumps, as does the study of almost anything; but I am not wholly convinced by Stigler's argument that conservatism is somehow more *intelligent* than radicalism. I would rather raise another, less elegant, possibility as to why economists are predominantly conservative in their outlooks. This is because economists tend to be located in the upper echelons of the pyramid of incomes and thus tend to share, consciously or otherwise, the conserving attitude that is characteristic of top echelons in all societies. I do not mean that economists are the spineless servants of the very rich. But in 1967 the average income of associate professors of economics (the middle group of academic rankings) was $14,000 and the average income of a "superior" full professor was $21,000. That was sufficient to place associate professors in the top 10 percent of income receivers in the country, and superior full professors in the top 2 percent. I do not see why it should be doubted that economists, like all groups, take on the values and standards of the socioeconomic milieu in which they live.

Yet, what is generally true of the group as a whole is certainly not true of each and every member of it. If, as both Professor Stigler and I believe, the economics profession is marked by a general conservatism of views, there are still economists enough, including some very eminent ones, who do not share the prevailing attitude. What the essays in Part 1 of this reader will show is that economics can be a formidable vehicle of social criticism and a powerful agent of social change. Hence, it is not the discipline of economics, diminishing marginal utility and all, that can be held responsible for its lack of relevance, if we mean by this its frequently observed failure to direct its attention to important social issues. The fault lies rather with the reluctance of many of its practitioners to use their economic skills for purposes that may be intellectually uncomfortable, or politically risky, or simply out-of-step with their colleagues. To that extent, the irrelevance of which students complain lies not within the discipline of economics but within that of sociology, and the cure for the problem lies in the determination of these students to put their own skills to good use when they take the places of their former instructors.

The Limitations of Economics

But there is a second, and perhaps deeper, meaning to the charge that economics is "irrelevant." It is that the results produced by the application of conventional economics too often have no usefulness—that the answers that economics gives to the problems to which it does address itself are frequently untrustworthy as guides to social policy.

This is a charge that, as we shall shortly see, contains what I believe to be an important core of truth. Yet, before we examine the limits beyond which economic reasoning cannot be relied upon, it is important to establish the things that economics can do and the extent to which it can be put to practical use.

The dividing line, as I see it, that separates what economics can do from what it cannot, lies between the usefulness of economics in explaining the structural characteristics of a market economy, and its relative uselessness in predicting how a market economy will behave in a given instance. To put it differently, economics is extremely relevant when we want to know how the economy is constructed, so that we can trace the numerous possible connections between one part and another, but usually "irrelevant" (by which I mean unreliable) if we want to know exactly which of these connections will be triggered off by a particular economic stimulus.

We shall consider in a moment the reasons for this predictive failing of economics. But at this juncture, while we are still concerned with the positive, relevant aspects of conventional economic thought, it is important to emphasize the enormous contribution that the structural insights of economics offer us. Perhaps only someone who can remember the intellectual confusion of the Great Depression, or the sense of heretical shock that greeted President Kennedy's proposal to spur economic growth by deliberately incurring a federal budgetary deficit, can fully appreciate the gain that has been won by the gradual clarification of the macrostructure of the economy. For the first time in the history of industrial society, we have finally grasped the nature of the mechanism by which the critical aggregates of employment and income are determined. Even if we still cannot manipulate that mechanism very well, the gain in intellectual clarity in itself constitutes the strongest single claim that conventional economics has for its own relevance, and it is a powerful claim indeed.

Microeconomics is not far behind, moreover, in claiming for itself a similar relevance. As with macroeconomics, microeconomics is also a poor guide for prediction. But without its general structural concepts—its ideas of demand and supply, of short and long run, of elasticity and inelasticity, of marginal and average costs and revenues and products—the operations of a market system would be virtually impossible to conceive, much less to control. Since all economic systems, socialism included, depend to some extent on the operation of a market mechanism, the linkages revealed by microeconomic analysis are indispensable for the understanding of all modern industrial systems. Whether it is to determine the best way to alleviate poverty, or to curb pollution, or to distribute scarce resources, or to judge the incidence of a tax, or to gauge the effects of raising the price in a nationalized industry, it is to the apparatus of microeconomics with its criss-crossed lines and its bowl-shaped curves, that we must turn if we are to think clearly about the consequences of our actions.

The articles in the second section of this reader are selected to display the power of economic reasoning in action, and I doubt that anyone can read through these selections and not be impressed with the clarification that economic analysis can bring to tangled social problems. Yet I do not want to leave the impression that economics, in its conventional use, is therefore always relevant, in the sense of giving us clear answers and reliable solutions. Rather, as I have already stated, I believe that there are very important limits on the extent of the reasoning power of economics, and it is to these limits that I will now turn.

I have already indicated one of the limits—the poor capabilities of economics as a predictive science. One reason for this, with which we are all familiar, is the inability of the discipline to handle more than a limited number of variables at one time. Economics is forced to approach the complexity of real-life situations exactly as we do in the classroom, on a *ceteris paribus*—other things being equal—basis. But the one-thing-at-a-time approach often breaks down hopelessly when we try to apply it to the world. Economics calculates its predictions as if the disturbance it studies were the only stone dropped in a pond; whereas in fact, of course, the surface of the pond is covered with the expanding concentric waves of a hundred disturbances. It is hardly surprising that the patterns of the disturbance in which we are interested become confused with or indistinguishable from those of other disturbances, and that our predictions lose their sharpness accordingly.

There is, however, a deeper reason for the unreliability of economic prediction than this. It is that the entire predictive capability of macro- and micro-theory rests on a highly simplified set of assumptions with regard to economic activity itself. These assumptions tell us that human beings constantly try to maximize their receipts (or to minimize their expenditures) as the paramount "behavior directives" in the course of their daily lives. To the extent that firms or factors or consumers do not obey these assumptions—that is, to the extent that they do not constantly strive to move to the frontiers of their production possibilities or their indifference maps—economics loses virtually all of its ability to predict the effects of stimuli on the economic system. In that case, for example, we can no longer state with certainty that a rise in price will result in a fall in the quantity demanded and an increase in the quantity supplied, for both of these classical behavior patterns are nothing but maximization in action.

Do we actually maximize? The concept itself is full of ambiguities. Maximize what, over what period of time? If we define maximization to mean "psychic income" or "satisfactions," then the concept loses its predictive power because *any* course of action may be said to lead to maximum "well-being," since we have no objective measure of whether that well-being is really maximized or not. On the other hand, if we define maximization to mean something specific, such as cash income, then we encounter a problem with regard to predictions over any period of time but the shortest run. A giant corporation, consciously trying to maximize its income over a period of ten years, may rationally decide to undertake any number of actions—raising prices, lowering them, increasing or decreasing its current investment—depending on how it interprets the future. In this case, maximization may accurately enough describe the state of mind of the management, but it is of little use in foretelling exactly what management will do.

It is because of these difficulties that economics is much better at describing the *consequences* of various paths that corporations or consumers may follow, than in predicting exactly which they will in fact elect to take. But there is a still more troublesome limit to its power of prediction. For even if we could define maximization in such a clear-cut way that we knew precisely what course of action it would enjoin, economic theory still finds itself stymied before the awkward fact that maximization can lead to different—indeed, contradictory—behavior in different expectational settings.

Ordinarily, as we have just said, a factor or a firm will try to maximize its income by selling more of a commodity when its price goes up and less when its price goes down. But what if the rise in price leads us to believe that prices will continue to rise in the future? In that case, the road to maximization lies in a different direction, namely in holding back on our offerings today so that they can be sold at a better price tomorrow, or in buying more today before the price goes up further. In a word, when expectations tell us that an observed change in price will continue in the same direction, then the rational pursuit of maximum income bids us to behave in exactly the contrary fashion to that which we do "normally."

If this abnormal kind of economic behavior were limited to occasional periods of extreme crisis, we might relegate it to a footnote. But unfortunately, precisely this kind of behavior is all too normal, whenever the economy is moving from one prevailing psychology, whether boom or bust, to another. Then, typically, markets become unstable just because expectations change, and the predictive capabilities of economics diminish accordingly.[2] That is why even the most sophisticated econometric models of the economy do well only as long as the basic direction of economic movement remains the same, but fail badly in telling us the one thing we want to know; that is, when that basic direction itself will change.

[2]The most searching critique of the shortcomings of the conventional economics can be found in Adolph Lowe, *On Economic Knowledge* (Harper & Row, 1965, paperback, 1970).

Thus, one endemic shortcoming of economic reasoning is its inability to alert us to the timing of economic events. But there is a second quite different limitation to economic theory that interferes with its predictive capability from another angle. It is that economic reasoning is unable to connect changes in the economic variables with changes in the political and social spheres of social activity. As a result, economics makes its predictions as if the stimuli and constraints of the market were the only forces impinging on the activities of men, ignoring entirely the social and political and psychological consequences of economic action. To put the matter differently, conventional economics deals with the economy as if it were only a mechanism for allocating goods and services, and overlooks the fact that the economy is also a mechanism for allocating privilege and power.

As a result, economic predictions often fail because they do not anticipate the "feedbacks" of noneconomic activity. Typically, for instance, economic theory will project a growth path by calculating the effects of labor and capital inputs, capital-output ratios, and so forth, in this way arriving at a course of economic output in the future. But the trouble with these projections is that economic theory does not take into account the noneconomic changes that the growth process itself may initiate. Economics does not, for example, connect the trajectory of growth with social frictions to which the growth process may give rise, or with political resistances that may be encountered if growth brings a shift in income as between regions or social groups. Nor does it ask whether a growing level of income may alter our life-styles or our working habits in such a way as to change our labor inputs. In a word, economic theory gives us a picture of change from which the political or sociological elements have been rigorously excluded, although it is just these factors that are often all-important in determining the ultimate results of economic change itself.

This restricted scope of economic vision serves to limit the relevance of economic theorizing even more severely than its inability to handle the vagaries of economic behavior. Indeed, here is where the freshman's unease about the "abtractness" of economics comes home with a vengeance. But at this level of analysis the student's objections are not so easily brushed aside. No one denies that abstraction is an essential precondition for a social science if it is to reduce the complexity of the real world to manageable proportions. But we can now see that the sharper and clearer the abstract model we create, the less "interdisciplinary" that model tends to be. Thus we learn how to handle the idea of a "firm," but only by blotting out the political and sociological attributes of real corporations; or we invent the very convenient fiction of a "factor of production," but only at the cost of losing to sight the existence of individuals who are also voters and members of social classes.

The fault, however, is not just that of a failure of nerve on the part of economists. *The essential problem is that we do not know the nature of these subtle linkages between the economic mechanism and the political and social spheres of activity.* What we lack, in a word, is a unifying theory of social change in which the distinctions of "economics" and "sociology" and "political science" would yield to a new "holistic" science of society. As we shall see in our next section, there was a time when economics seemed to be close to such a holistic science. It is not today. Instead we stand impotent before the problem of understanding how to integrate our knowledge of the economic structure and of economic behavior (unpredictable though the latter often is), with a corresponding knowledge of political or sociological structures or of political or social behavior. The discovery of such a new integrating model or paradigm would be the greatest triumph of social science in our time, but at the moment no such paradigm exists. As a result, we must admit to a profound limitation to economic analysis for which no solution is now in sight.

The Relevance of Economic Philosophy

These considerations bring us to the last meaning that we can attach to the word *relevance*—the possibility of using economics as a guide for social philosophy, in the sense of helping us to understand the direction in which our social system is headed, or still more important, the direction in which it should head.

In the light of the severe limitations that we have put upon the predictive power of economics, can we really look to economics as a reliable guide for the future? The answer is necessarily disconcerting. We cannot. At best, an economist who postulates a rationale for the historic setting of our time or who projects the shape of society into the future is engaged in no more than a kind of controlled speculation. That these speculations can be both eloquent and plausible we shall leave for the reader to discover for himself in Part 3 of this book. But it would be wrong to pretend that even at their most convincing these speculations attain the status of genuine scientific effort, at least in the meaning that economics usually arrogates to that word.

This is an important matter to which we shall revert at the very conclusion of this essay. But meanwhile, for students who have read the works of Smith, Ricardo, Mill, or Marx, this must seem like a serious retreat for economics. For surely the great classical writers did not regard their large-scale economic philosophies as mere "controlled speculations." In their hands economics seemed capable of presenting a perspective on the present and the future in full accord with the scientific canons of their day. Why, then were they able to create economic philosophies of greater power than we can?

From the vantage point of contemporary history, we can discern two attributes of classical economic thought from which this extraordinary self-assurance emanates. One of these, which is frequently overlooked, is the strong feeling of social destination that infuses all the classical writers. Smith, Ricardo, Malthus, Mill, and above all Marx, firmly believed that they knew the direction in which society was heading, and moreover they strongly approved of that destination as being in the best interests of mankind. Thus, economics became for them not alone an objective explanation of the "laws of motion" of their respective economic societies, but also an instrument to assist the evolution of those societies in the various directions in which they wished them to hurry.

A second common attribute of their thought was their frank willingness to discuss their societies from the point of view of class composition and conflict. In place of the neutral "factors of production" with which modern theory deals, the classical writers spoke openly of a contest of landlords, workers, and capitalists, so that their theories of distribution (which were intimately intertwined with their theories of growth) were also guides to major political and social tensions within their societies. And whereas the outcome of the struggle among the classes was differently diagnosed by each writer, according to his differing assessments and assumptions regarding resources, demographic behavior, technology, and the psychology of the social classes, in every instance his pursuit of the logic of economic interaction led him directly to an associated drama of political and social change.

In our own day, both these underlying premises of classical reasoning have lost much of their erstwhile force. The blows of 20th-century history, devastating for the prospects of liberal capitalism and orthodox socialism alike, have largely obscured the vista of welcome historic destination that unified and fortified so much of classical thought. Today the great majority of social scientists, economists included, stand before the realities of 20th-century technology, bureaucracy, nationalism, and militarism with a sense of genuine perplexity, or even despair, that blurs the vision of even the boldest of them.

Then, too, the increased complexity and growing modest affluence of Western society have equally undermined the second of the premises of classical analysis—that the dynamics of social change could be directly predicted from the clash of social classes. In our day, the once decisive clash of classes has given way to the cohesion of a "mass society" in which the sources of social conflict take on wholly new forms, such as the conflict between generations. As a result, even the most fully worked-out philosophy of historic change and social evolution—the imposing structure of Marxism—finds itself in need of rethinking its traditional views in the light of present-day realities.[3]

Against these vast historic changes, it is hardly surprising that economics has lost the self-assurance of a former age. The problem of constructing a plausible model of social change is much more difficult in our day than in a simpler age, for all the reasons we have discussed in the previous section as well as in this one. Yet it is one thing to take cognizance of the difficulties of a task, and another to abandon it. Rarely has there been a period of history as much in need of illumination as our own, and however partial or uncertain, the controlled speculations of economic thought, meshed as best they can be with political and sociological analysis, still constitute the best response that we can make to our human situation.

Perhaps in the end, the answer to this impasse of the social sciences lies in a new appraisal of the relevance of *science* itself. When we said before that economics could offer no foresight that could be given the name "scientific," we may have inadvertently opened the direction in which to seek the new paradigm of social unity that we need. The word "scientific," as we commonly use it, refers today to a rigorous model of a mathematical kind from which all considerations of social values have been carefully excluded. In the great question of human destination, however, values must surely occupy a central place: the future is meaningful because it offers us choice. Perhaps, then, the very aim of economic philosophy as a "scientific" guide to the future must give way to economic philosophy as a consciously value-laden guide—a guide that uses the enormous powers of scientific analysis, not to predict the future, but to assist society in reaching the goals that it has elected to pursue. In such a basic reorientation of the discipline, economics would become the handmaiden of politics, advising us of the institutional and behavioral and technical conditions necessary to achieve a destination that society has chosen through its political processes. Such a far-reaching suggestion takes us well beyond the confines of this essay, although not, I am glad to say, beyond the confines of what may ultimately be most relevant for economic thought.[4]

[3]The evolution of Marxist thought can be followed in such books as Ernest Mandel's *Marxian Economic Theory* (see the last essay in this collection), Ralph Milliband's *The State in Capitalist Society,* or in the various contributions to Erich Fromm's *Socialist Humanism.*

[4]See R. Heilbroner, "On the Possibility of a Political Economics," *Journal of Economic Issues,* December 1970, and "On the Limited Relevance of Economics," *The Public Interest,* Fall, 1970.

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