



# Culture, Social Norms and Economics

## Volume I Economic Behaviour

*Edited by*

**Mark Casson**

*Professor of Economics, University of Reading, UK*

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# Introduction

*Mark Casson*

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## 1. The Scope and Purpose of this Book

Economists are often accused of failing to take proper account of culture and social norms in their explanation of human behaviour. The stereotype economist is the practitioner of a 'dismal science' in which the law of competition regulates the behaviour of selfish individuals. Compared to other social scientists, the economist is committed to a very narrow view of human nature which is pessimistic about the prospects for improving social welfare. Other social sciences suggest that cultural change, and in particular the raising of social norms, will lead to higher standards of behaviour. The evolution of higher norms thus offers a direct route to the improvement of social welfare – a route which for the stereotype economist remains permanently blocked.

Not all economists conform to this stereotype, however. This book highlights recent economic research which adopts a much broader and more optimistic view of human motivation. There is an enormous range of literature which could have been considered for inclusion. A decision was taken at an early stage to restrict attention mainly to the writings of either professional economists or of non-economists who none the less employ a distinctively economic style of reasoning. A few papers are included because, although they do not make explicit use of economic reasoning, the ideas they contain can readily be formulated in economic terms. It was also decided to exclude related topics such as economic psychology which are covered by other volumes in this series. Within the literature so defined, the final selection was governed by the intellectual qualities of individual papers, their brevity (since space is scarce), and the desire to include a representative piece on every major topic. It was originally hoped to include one example of the work of every major writer in this field, but unfortunately this proved impossible without considerable overlap.

This introduction is organized into three main parts. The first (sections 1–5) is mainly concerned with the issue 'Where are we coming from?' It considers how the present narrow concept of 'economic man' came into being, and what needs to be done to escape from its mental straitjacket. The second part (sections 6–12) addresses the question 'Where are we now?' It summarizes the modern literature and takes stock of recent developments. The final part (sections 13–17) asks 'Where are we going?'. It sketches out one possible scenario of how a more insightful model of 'economic man' may be developed.

## 2. The Economic Approach to Culture

There is already a vast literature on culture generated by sociologists, anthropologists and social historians. As indicated above, this book focuses mainly on economic research. The

defining characteristic of the economic approach is the use of the rational action model of human behaviour (see Blaug, 1980). According to this model, individuals have preferences which rank all the alternatives that they perceive in a consistent way. They collect information to assess the feasibility of these alternatives, and then select the best of the feasible ones. The rational action model is introspectively plausible insofar as it stresses the intentionality of actions, and the existence at the time of action of a definite expectation of what the outcome will be. It is less plausible in the sense that it suggests that a large amount of computation is associated with each decision. Economists usually respond to this criticism by arguing that *on average* people behave as if they were carrying out such computations, even though no single individual is conscious of having done so. A more sophisticated response is to argue that individuals respond to the costliness of information by economizing on the amount of information that they use. The amount of computation is tailored to the importance of the decision, which is why trivial decisions are taken with relatively little thought. This approach, based on the economics of information, is particularly useful in explaining the behaviour of people within organizations (Casson, 1997).

While rational action is sufficient to explain the behaviour of a single isolated individual ('Robinson Crusoe' in standard economics texts), it needs to be supplemented by some other principle where a group of people is concerned. This is because the actions planned by different individuals may be incompatible with each other. There needs to be some mechanism which allows each individual to adjust their perception of what is feasible to allow for the impact upon them of the decisions that other individuals are about to make. This is a complex information-processing problem. To reduce the problem to manageable proportions economists normally invoke the principle of equilibrium. This principle asserts that the expectations that individuals form before they act are consistent with the actions of other people, even though they do not necessarily know what those actions are. This ensures that the actions of different people harmonize with each other so that, in retrospect, no one wishes to change the decision they have made.

In forming their expectations people do not normally need to know about every aspect of other people's plans. It is usually sufficient for them simply to know their aggregate effect. This means, though, that there must be some mechanism to aggregate the effects of individuals' provisional plans, and to communicate the results back to individuals so that they can modify their plans if necessary (Hayek, 1937). In some situations, such as that of bilateral monopoly, there is no obvious equilibrating mechanism. In other situations, such as competitive markets, publicly quoted prices play the equilibrating role. A set of competitive equilibrium prices summarizes all the aspects of other people's plans that individuals need to know about in order to optimize their own behaviour. Social situations in which people exchange gossip or reciprocate gifts typically occupy an intermediate position. There is no explicit price, in the sense that nothing is formally bought and sold, but there may, nevertheless, be an 'implicit price' which supports an equilibrium. The price is implicit in the sense that every one is agreed how much sacrifice, on average, is entailed in gaining some favour. The implicit price represents a consensus view of the situation. It is an equilibrium price insofar as it reconciles each individual's plans with those of other people.

### **3. From Selfishness to Altruism**

The narrowness of vision associated with the dismal science is not a consequence of adopting the principles of rational action and equilibrium, but of assuming that rational action is directed towards purely selfish and materialistic ends. Rationality itself is perfectly compatible with an optimistic view of human nature – indeed, in the early nineteenth century European intellectuals regarded rationality (which they defined as freedom from superstition as well as the ability to calculate) as the key to social progress. From the more formal standpoint of modern economic theory, the principle of rational action applies just as much to individuals whose aims are altruistic, or even purely spiritual, as it does to those whose aims are selfish and materialistic. Of course, theory must link these ultimate altruistic and spiritual ends to more proximate ends in order to explain people's everyday behaviour. This is done by specifying an appropriate transmission mechanism. In the case of the altruist, the purchase of goods for the purpose of making gifts, and their subsequent transfer, links his purchases to their intended effect on other people's welfare. In the case of a person pursuing spiritual goals, the symbolic significance of goods – especially in the context of social and religious ritual – links their purchase to the individual's strategy for acquiring peace of mind (Douglas, 1970).

But if selfishness is not essential to the theory then why have economists chosen to focus so narrowly on selfish and material ends? There are four main reasons. The first is that selfish preferences are easier to model than altruistic preferences because only one individual is involved. To model altruism it is necessary to evaluate the different ways in which empathy for other people can manifest itself. It is necessary to address the difficult question of how far an altruist can reasonably claim to know the preferences of his intended beneficiaries. One way out of this difficulty is to assume that altruists wish to benefit other people in general, so that each altruist is effectively concerned with only two people – himself, and a composite person who represents the rest of society (Margolis, 1982). Each individual formulates his own view of how this representative person feels. Although this specification of preferences is still more complex than a purely selfish one, the additional complexity is of manageable proportions.

The problem of specifying altruistic preferences leads in turn to the question of whether altruists really do feel empathy for other people, or whether they simply derive a hypocritical sense of satisfaction from manipulating the behaviour of other people through the gifts that they provide. Is altruism just a distorted form of self-interest, in other words? From a purely formal point of view it does not really matter whether it is or not. Nevertheless, the philosophical problems raised by questions of this nature explain why many economists maintain that altruism is a complicating factor that a parsimonious model of human nature should really do without.

A third reason is that selfish preferences tend to focus on material consumption, and material consumption is easier to measure than other forms of consumption. It naturally lends itself to quantification, and the tangibility of the goods consumed makes these quantities relatively easy to observe. This in turn makes propositions about material preferences easy to test. By contrast, altruistic preferences are often concerned with the provision of intangible services, such as the emotional security that a parent attempts to provide for his child. Since, however, these intangible services feed through to generate tangible effects

elsewhere (for example, in the behaviour of the child), it is still possible to formulate preferences in a testable way. In any case, the advantages of quantification are easily overstated, since many qualitative variables can be expressed using categorization instead. To some extent, the emphasis on material consumption in conventional economics is simply a legacy of the scientific materialism of the late nineteenth century, which was in fashion at the time that the mathematical utility theory used by modern economists was being refined. In this respect, a change in the professional attitude towards the specification of the utility function is long overdue.

Finally, the assumption of selfishness seems particularly appropriate in the context of competitive markets. Competition works by each person playing other people off against each other in order to secure more favourable terms for themselves. Each buyer plays off different sellers against each other, whilst at the same time each seller plays off the different buyers against each other. The simplest motivation for such behaviour is a selfish concern to obtain the best possible deal, even though this is against the interests of other people. The traditional preoccupation of economists with explaining how markets work has therefore led them to assume that selfishness is pervasive because this is the simplest basis on which to construct a model of competitive market behaviour. From this perspective, the typical economist is not really interested in people at all, but only in a particular type of institution – the market – which is characterized by an unusually impersonal and competitive form of social relation. This means, though, that when it comes to explaining other social structures, where co-operation is stronger and competition is less intense, it is helpful to relax the assumption of selfishness on which the competitive market model is based.

#### **4. Beyond the Market**

Economists' preoccupation with markets has been unfortunate in other ways as well. It has led some economists to believe that the concept of equilibrium is somehow logically prior to, or at least on an equal footing with, the principle of rational action whereas, if anything, the opposite is actually the case. Rational action is a principle that applies almost universally within the social sciences. In whatever social context human motivation is discussed, rational action modelling has a contribution to make. The concept of equilibrium, however, is of more restricted scope. Few social systems have equilibrium tendencies as strong as those of a competitive market. Even where social equilibria exist, they may not be unique. Emphasizing equilibrium rather than rational action therefore understates the scope of economic reasoning by highlighting some of its major limitations. It thereby discourages people from applying rational action modelling to social situations where it is useful simply because they recognize that the equilibrium tendencies are weak.

Emphasis on markets has also led some economists to believe that the market is the only form of co-ordinating mechanism that merits serious study. Although economists have always grudgingly recognized that governments and firms have co-ordinating capabilities as well, they have been reluctant to scrutinize their internal mechanisms as closely as they scrutinize the role of competition in the market. Yet governments, firms and markets are all just alternative forms of co-ordinating mechanism (Coase, 1937). To understand why some activities are co-ordinated by governments, some by firms, and others by markets, it is



necessary to understand the internal workings of each type of institution. Only then can a proper comparison of their effectiveness be made.

## **5. The Social Basis of the Market Process**

Focusing on government and firms highlights the importance of social interaction in the co-ordination process. It is by sharing information with each other, in both formal committees and informal gatherings, that managers and bureaucrats are able to take complex decisions. Reflecting further on this role of social interaction shows that there are many other institutions – such as clubs, societies, and local communities – which participate in the co-ordination process. These other institutions typically operate – like government – on a non-profit basis. But – unlike government – they operate on a voluntary basis too, relying on the goodwill of their members to get most of the work done.

Finally, consideration of the social dimension of co-ordination reveals that, in important respects, markets are social institutions too. Many markets for consumer goods are established by innovating firms. Because consumers interact socially, knowledge of a new product spreads by word of mouth. This stimulates the growth of market demand – especially when consumption of the product becomes a sign of social status. The diffusion of information through social networks is important on the supply side of the market too. As information about the innovator's profits spreads throughout the business community, so imitators begin to appear. Competition between the innovator and the imitators drives down prices and eventually restores profits in the industry to a normal level.

Although firms in the same industry compete, they may also co-operate – for example, in lobbying for 'infant industry' protection, or pressing for the abolition of restrictions that inhibit further growth in demand for the good. Many organized commodity markets, in fact, originate not with individual innovation, but with collective innovation – they begin as clubs formed by dealers, whose members agree to meet at a certain place and to trade under certain rules. Only later do these clubs acquire formal legal recognition as self-regulating institutions. By focusing on markets that are already well established, economists have failed to recognize the importance of social processes in bringing these markets into being in the first place. If economists paid more attention to the origins of contemporary institutions such as markets, they would not only acquire a better understanding of the social dynamics of institutional innovation, but they would also achieve a better understanding of how markets work today.

## **6. The Political Economy Tradition**

To understand the origins of institutions properly it is important to have an adequate theory of human motivation. As noted at the outset, the purpose of this book is to illustrate the progress that has already been made by economists in moving towards a broader view of this subject. The book is structured into ten parts. Volume I (comprising four parts) is mainly concerned with modelling the social and cultural aspects of individual behaviour, whilst Volume II (comprising six parts) focuses on the organization of co-operation within

the economic system, and on the role of culture in supporting this.

Creating a broader view of human motivation within economics does not involve beginning from scratch. A broad perspective on human motivation can be found in the early literature of political economy. Part I of Volume I explains the insights into human motivation, the holistic view of social science, and the progressive view of society that inspired the economic writers of the Scottish Enlightenment. Aspects of this vision continued to inspire leading British scholars such as John Stuart Mill, John Elliott Cairnes and Henry Sidgwick, right down to the time of Alfred Marshall. While these scholars valued the technical contributions made by David Ricardo (and subsequently by William Stanley Jevons), they never fell completely under the influence of radical utilitarians like Jeremy Bentham, despite the growing influence of Bentham's legacy on this technical work. They did not believe, as Bentham did, that the enormous complexities of social organization amongst selfish people could be successfully tackled by simple incentive mechanisms embodied in formal legal rules. This affirmation of the broader view is particularly clear in the case of Mill who successfully freed himself from the Benthamite utilitarianism imparted by his father to reassert the broader view in his later work.

In contrast to many leading economists of today, these political economists saw no need to distinguish sharply between 'rigorous' economic theory and 'non-rigorous' social theory, nor were they so pessimistic about the possibilities for social reform as modern economists have become. Contemporary attitudes amongst economists can, to some extent, be justified as a reaction against the excesses of twentieth-century sociological theory, which has been preoccupied more with ideological debate than with fixing an agenda for sustained empirical research. On the other hand, it must be recognized that both sociology and political science 'spun off' from political economy partly out of frustration with the increasingly narrow intellectual concerns of the economics profession. Furthermore, part of the political radicalism of the sociologists was due to the fact that, by the turn of the present century, many professional economists had aligned themselves ideologically with the principle of *laissez faire*. The modern economics profession is thus essentially what remains of this rump of *laissez faire* economists three or four generations after those who were seriously interested in the human dimension of economic problem quit to go elsewhere.

## 7. Modelling Individual Preferences

The remainder of Volume I (Parts II–IV) addresses various aspects of modelling individual preferences when the assumption of selfishness is dropped. Part II discusses altruism and envy, in the form of positive or negative feelings about the consumption patterns of other people. The basic aim of these models is to capture the pain and pleasure to be earned by vicarious participation in the consumption activities of other people.

An important focus of envy relates to the social status enjoyed by other people. Status encourages people to think in terms of relative rather than absolute levels of consumption, and in particular about where they stand in the overall ranking of consumption levels within society. Thus when they obtain an increase in income, people are even happier if others do not share their good fortune. Status is one of the few effects discussed by political economists that has experienced a significant revival in recent years. Status effects were widely

discussed amongst policy-makers in the 1970s – in the context of ‘relative deprivation’ amongst the poor, the bargaining tactics of trade union negotiators in raising their members’ pay relative to that of other groups, and so on. Unfortunately, however, interest in status appears to have subsided during the 1980s and 1990s, partly because of prevailing political ideology in the US and UK.

Advocates of a free market economy often attack status as a source of rigidity, failing to recognize that in certain circumstances status mechanisms can in fact augment conventional market forces in a useful way. Because of the limitations of the legal system, conventional markets are often costly to use and invariably incomplete in their scope. There is thus an opportunity for other mechanisms, such as status, to help to ‘complete the market’. Whether status effects can do so depends upon how status is ascribed. If it is ascribed by birth, or some other characteristic that the individual cannot control, then status effects are certainly of limited use. But when status is ascribed on the basis of performing socially useful tasks which are difficult to reward through conventional market mechanisms, then stimulating the desire to earn status can stimulate the supply of effort too. Thus the provision of public goods, such as useful inventions, whose value is difficult to appropriate through contractual means, may be stimulated by rewarding inventors with status instead.

There is, however a negative side to status. An improvement in one person’s status usually implies a reduction in someone else’s status, so that the search for status tends to be a zero-sum game. If everyone agreed that no one would seek status then everyone might well be better off. But given that such agreements are difficult to enforce, it is probably easier to harness it for motivating public service, in the manner described above, than to try to suppress it altogether.

Many economists, though, continue to believe that status is too much of a complicating factor to warrant taking seriously, despite abundant evidence that it influences demand for fashion goods, affects the occupational choices of school-leavers, and continues to be a major factor in conflicts over pay. The articles reprinted here suggest, however, that the modelling of status does not introduce as many complications as it might be thought, and that simple testable propositions can be derived by incorporating the desire for status into preferences. Indeed, once the techniques of modelling status have been mastered, status effects may well turn out to be by far the simplest way of explaining a range of otherwise problematic economic phenomena.

If modelling status is complicated, then modelling the economics of self-control (Part IV) is potentially more complicated still. Once again, the stereotype economist will ask what is to be gained from an exercise of this kind. The main advantage of a theory of self-control is that it can ‘rationalize’ apparently quite irrational behaviour. For a start, it can explain why individual behaviour may be apparently inconsistent over time. People say one thing, quite sincerely, and then do exactly the opposite, or they follow one action with another that seems to defeat the purpose of the first. Such behaviour can be explained in terms of lapses of self-control. If self-control depends upon a scarce resource, then lapses may be unavoidable when supplies of this resource run out. In the short run, all a rational economic agent can do is to allocate the scarce resource so that the lapses that do occur cause as little damage as possible. In the long run, the individual may be able to invest in ‘personal development’ in order to acquire greater reserves of self-control.

Perhaps the most significant application of a theory of self-control, however, is to explain

why people deliberately 'tie their own hands'. For example, they may ask a friend to control their own behaviour (such as their intake of alcoholic drinks at a party) because they are afraid that they may be unable to exercise sufficient control themselves. People may support campaigns for censorship on the grounds that they do not wish to be corrupted at some future time when their self-control is relatively weak. The theory explains why people may not desire to maximize their range of choice, but rather to restrict it; a self-imposed restriction may be rational for a person who believes that, while their self-control is currently strong, they need to insure themselves against the consequences of it becoming weak.

## **8. Co-operation**

Part I of Volume II examines how cultural values affect the incentive to co-operate. It is often suggested that co-operation can be explained purely in terms of enlightened self-interest. The prospect of being punished by your victim in some future repetition of your encounter with them may well be sufficient to encourage good behaviour at the outset (Kreps and Wilson, 1982). In particular, if you believe that other people behave according to the principle of 'tit-for-tat', then it often pays to adopt the strategy of 'tit-for-tat' yourself. Tit-for-tat therefore becomes an equilibrium strategy for the group.

But what happens if a repeated encounter is unlikely? Tit-for-tat becomes inoperative in this case, because the opportunity to punish disappears. As a result, cheating may well pay instead. Indeed, if everyone else is going to cheat then it is doubly important that when you encounter them you cheat yourself. If you do not wish to cheat then you simply avoid contact with other people. In this way all economic activities based on a division of labour – which means all activities involving employment or trade – come to a stop.

To restart activity under these circumstances people need to have credible grounds for believing that others will be honest even if they have a material incentive to cheat. One reason that others may be honest is that they will feel guilty if they cheat. If everyone knows that everyone else feels this way then everyone can afford to be honest because everyone else will be honest too. In this way a 'high-trust' equilibrium can be sustained by self-fulfilling beliefs in the integrity of other people.

Some economists appear to be mystified by arguments of this kind because they are used to premising their analysis on the existence of a system of law. It is true that if every form of cheating was covered by a perfect system of law then cheating could in principle be eliminated at a stroke. But, in reality, the law is a social institution which itself needs trust in order to sustain it. A legal system cannot work efficiently when the police or the judiciary is corrupt. The law is essentially an intermediating institution, allowing people who cannot trust each other to trust the law instead. The law conserves a scarce resource like integrity by concentrating honest people on the resolution of disputes between people less honest than themselves. But the arrangement still requires a core of honest people to make it work.

The law can be a very expensive intermediating mechanism. The law makes intensive use of information, and consequently information costs are a major constraint on the legal process. It is not just a matter of the cost of collecting evidence, but also the cost of testing its veracity given the strong incentive for those who have cheated to lie about what they have done. Indeed, the fairer the law attempts to be, the more expensive it becomes. Accurate



judgments delivered by formal court proceedings are much more costly to arrive at than the 'rough justice' of the 'kangaroo court'. This suggests that for cost-effective co-operation, alternatives to the law must be explored.

## **9. Social Alternatives to the Law**

Parts II and III of Volume II discuss two alternatives to the law: intermediation by society, in the form of peer regard, and intermediation by a leader to whom others naturally defer. The first mechanism tends to rely heavily on custom and conformity; it works best in small groups with a stable membership and regular face-to-face communication. Because it depends on custom, however, it is not very good at adapting to new sets of circumstances that arise. Although custom is more than just the 'dead hand of the past', its legitimacy certainly derives to some extent from the fact that no one can remember when things were done a different way. Thus while custom can adapt, there are definite limits to the speed at which this can take place.

The second mechanism – leadership – is much more flexible. A leader can act in an entrepreneurial way. He has the authority to exercise discretion in dealing with an unprecedented situation. The disadvantage of leadership is that it may confer excessive power upon a single individual. In this respect, consultative leadership is normally superior to autocratic leadership, in the sense that a consultative leader pools opinions in order to synthesize information from different sources, whereas an autocratic leader does not. The autocrat relies only on those sources of information which he can directly consult himself. A consultative leader is also more likely to be altruistic because, through the process of consulting other people, he is likely to develop a sympathetic understanding of the effects of his actions upon people other than himself. Nevertheless, there may be certain crisis situations in which autocracy is preferable; when it is crucial to act quickly, but opinions are divided, whatever the autocrat decides to do may work better than a consultative decision.

## **10. Religion**

Parts IV and V address two specific aspects of culture – religious belief and entrepreneurship – each of which could easily justify a volume in its own right. There is plenty of evidence to suggest that people care about the kind of society in which they live, in the sense that they are willing to pay, through higher house prices and a higher cost of living, to move to countries, or to local communities, which offer a higher 'quality of life'. Concerns may well extend beyond the community, to embrace the global environment, and the future of humanity as a whole. Concern for the well-being of future generations is also reflected in parental concerns about the kind of society in which children will grow up to live. The widest concerns of all are religious concerns with the ultimate 'meaning of life', and with the prospects for an after-life. Such concerns are so strong that in polite society it may be unacceptable to raise them in casual conversation for fear of provoking an argument.

It would be strange indeed if people's passionate feelings about these issues were not reflected in their ordinary behaviour in some way. One indication of such feelings is the

magnitude of the voluntary contributions that people make to support churches, charities, and other 'good causes' of their choice. It is difficult to rationalize such giving – especially anonymous donations, which cannot be used to 'buy' status – without invoking some purely emotional reward that the donor receives. The existence of an altruistic impulse is not sufficient to explain why some societies sustain far higher levels of giving than others. It must be recognized that organized religion plays an important part in directing emotions not only into support for established beliefs about the after-life, but also into support for established ways of doing good. The standardization of belief through organized religion helps to realize economies of scale both in the provision of religious buildings and in the organization of charitable work as well.

Organized religion does not provide reassurance as a 'free good', however. The believer has to pay a price, and the voluntary donation to the church is only a part of that price. It is incorrect to suggest that churches merely 'sell' a form of supernatural reassurance in return for the gifts of the 'faithful'. For in most religions, deeds as well as gifts are required to buy reassurance, and the most important aspect of these deeds is they involve behaving honestly towards other people. Organized religion therefore provides powerful emotional incentives to live by functionally useful moral principles (see below), and thereby generates a potentially large economic surplus.

The survival of religious belief at a time when many progressive thinkers have expected such belief to wane is easily explained on these grounds. Religious belief confers economic value on communities in which it is strong. These communities prosper, and attract people from outside who assimilate the religion in order to participate fully in the economic gains. Conversely, societies in which religion decays need to replace it with other more expensive intermediating mechanisms. They need to strengthen their law, and promote 'communitarian' welfare policies, in order to combat the threat of rising crime – especially 'economic crimes' such as theft of property and cheating on trades. These costly mechanisms require either higher taxes, which undermine incentives to innovate and to work hard, or the displacement of public expenditure from services and infrastructure such as hospitals, schools and roads. These societies therefore become less attractive places in which to live, and those who can afford to, choose to leave. In this way societies that discard religion without putting another cost-effective institution in its place eventually decline. Amongst the societies that survive and prosper, religious observance is a prominent feature of the way of life.

## **11. Entrepreneurship**

Some scholars disagree strongly with arguments of this kind. They tend to place religion in the same category as custom, regarding it as an obstacle to change and innovation. They argue that, while it may be successful in binding people together, it binds them together inflexibly and makes them collectively resistant to change. In the very long run – over several centuries, for example – the societies that survive are those that are the most dynamic, it is claimed, rather than the ones that simply afford the highest quality of life. New York and Chicago may both be violent cities, it is said, but they are full of highly entrepreneurial people as well. The violence and the crime is a natural by-product of aggressive enterprise – and on balance, the crime is an acceptable price to pay. If the price

of crime were not acceptable then the entrepreneurs would move elsewhere. This implies that the only characteristic of a culture that matters in the long-run is whether it is entrepreneurial or not.

Such a one-dimensional view of culture cannot be sustained, however. Entrepreneurship can be highly competitive and individualistic, it is true, but it can also be co-operative and familistic as well. There is a limit to what a single entrepreneur can achieve without the support of other entrepreneurs in related lines of business undertaking investments that complement his own. An entrepreneur who cannot trust other people in related lines of business will be reluctant to share his plans with people he regards as his potential rivals, and as a result these people will be reluctant to expand their businesses in line with his because they are unsure about whether he would play them off against competitors if they did. On the other hand, an entrepreneur who trusts people in related lines of business can share his vision with them; provided that they know him, and are convinced that his judgement is sound, they will expand their businesses in line with his own. This second approach is, on average, likely to be more successful than the first. It is particularly easy to implement when trust is underpinned by family links, common schooling and, of course, shared religious commitments of the kind described above. This shows that custom and religion, far from inhibiting entrepreneurship, can be used to promote it by strengthening co-operation within the business community.

## **12. Culture and Economic Performance**

This result ties in quite nicely with the trend of recent political debate, in which the key ideological issue is no longer one of capitalism versus socialism. Instead, it is about what kind of capitalism works best. The erroneous idea that there is just one kind of capitalism, which is entrepreneurial but low-trust, has finally given way to the idea that there are at least two main forms of capitalism. One may be low trust, but the other is based on high-trust relations instead. In some cases these high-trust relations may be confined to a business elite – dominated, for example, by a small number of politically-networked family dynasties. In other cases, effective national leadership and a strong religious tradition may extend the network of trust to other social classes – notably professionals, skilled workers and the self-employed.

The larger the country, however, and the more diverse its industrial and commercial base, the more difficult it is for extended networks to operate effectively. As countries expand their borders, and population is increased through conquest, migration, high fertility, or longer life, social networks become less effective. They may still be effective at the regional level, but at the national level more impersonal and legalistic mechanisms have to be used instead. Thus during the nineteenth century the US evolved a low-trust competitive and legalistic culture in response to multicultural immigration and rapid urban growth – a culture significantly different from the high-trust culture of the early communities of New England. There may still be networks that operate at the national level in a large country, but if its society has become multicultural then they will be increasingly organized along ethnic lines.

If antagonisms develop between the different networks then the economic viability of the nation may be undermined. The antagonisms may be regional, religious or racial; or they

may be just class antagonisms – for example, between landowners and capitalists, or between capitalists and workers. A trend towards lower trust generated by class antagonisms can be observed at the end of the Victorian era in Britain, when the increasingly cosmopolitan nature of City financial trading, and the gradual stagnation of manufacturing industry, exacerbated class divisions between bankers and industrialists, and – more prominently – between industrialists and workers.

The legacy of these changes is that in many countries the region and the ethnic group appear to many people to be more viable economic units than the traditional nation state. This suggests that if nations are to survive without becoming increasingly repressive (through continual recourse to law) then political leaders need to do their very best to promote an inclusive high-trust culture. Merely preaching tolerance will not suffice; respect for cultural diversity needs to be combined with a focus on standardized core values – values such as honesty, loyalty and hard work. These core values will not only reinforce the cultures of the existing local networks but – most significantly – help to sustain co-operation between these networks too.

There is already growing recognition in many countries of the need for greater trust in supporting national business networks, but unfortunately many of the social mechanisms for engineering trust at the national level have been so neglected that they are in a poor state of repair. In the UK, for example, many of the key institutions – the monarchy, parliament, the established church – are currently held in low esteem. The same goes, unfortunately, for key professional groups such as teachers, doctors and civil servants too. More than mere incantation of the need for greater trust is required in order to rebuild the national networks on which they depend. There is still a long way to go in reviving or replacing these institutions in order to sustain a better kind of capitalism.

### **13. A Way Forward**

Can the literature reprinted in this book provide a coherent platform for institutional reform of this kind? What exactly is meant by the broader view of human motivation discussed at length above? Is this broader view really consistent with a parsimonious model of human behaviour based on the rational action principle? The papers reprinted in this volume provide only partial answers to these questions; none of them addresses the issues head-on. The clues that are distributed throughout these volumes can, however, be pieced together to provide an outline of an alternative model of human motivation to which they lead. The model should provide the platform for institutional re-design of the kind considered above.

What needs to be charted is an intellectual path that leads from a narrow and pessimistic view of human motivation to a broader and more optimistic one. So long as the rational action principle is retained intact while this transition is effected, the transition does not, strictly speaking, involve the abandonment of the concept of ‘economic man’. The basic technique remains the analysis of individual maximization over a well-defined field of choice. It is the specification of what is being maximized that is being changed. In addition, the cost of identifying the field of choice has to be recognized as well.

Greater social realism calls for more subtlety in the specification of the individual objectives. Greater subtlety unfortunately means greater complexity too, however. To control the degree



of complexity it is useful to think, as several writers have suggested, in terms of a hierarchy of objectives. Specifically, it may be useful to think in terms of three levels of objective. Each objective may be associated with a simple account of human behaviour. The three accounts of human motivation can be studied separately, and then synthesized to form the broader view of human behaviour that is required. The three building blocks for this broader view may be termed biological man, social man, and ethical man.

#### 14. Biological Man

The lowest level objective, it may be postulated, is survival (Maslow, 1970). So far as material consumption is concerned, a person who is motivated at the lowest level is pre-occupied with procuring basic needs such as food. The emphasis is on maintaining physiological equilibrium by replenishing stores of energy in the body when they become depleted. For this purpose simple feedback control mechanisms are employed. When energy reserves are depleted a feeling of hunger is generated, and this stimulates the desire for food. Survival also depends upon security. When danger threatens, the body is aroused so that it is prepared either to fight or to flee. As we shall see, feedback control can be interpreted as a rational response to the class of problems with which biological man has to deal.

Hunger and danger are both sensations that impinge on consciousness but there are, of course, many autonomous activities, such as heartbeat, and reflexes, such as swallowing, that people are not really aware of. People only become aware of them when something goes wrong. Feedback control is still in operation, however, because once health is threatened by malfunction, pain is generated, and consciousness is activated to plan remedial action.

The objective of survival is therefore pursued through a number of strategies, all of which are routinely implemented, often at a subconscious level. These strategies are all concerned with short-term responses to threatening situations of one kind or another – hunger, danger, illness, and so on. These situations recur on a regular basis, and it is therefore quite appropriate that they are handled using rules. When the same type of situation recurs frequently, the same pattern of response can be employed over and over again. It is therefore cheaper to devise a rule at the outset than to improvise a response every time the situation recurs.

In such situations it is also important that response is prompt, for procrastination only makes the threats more serious. Because investigation is time-consuming, it is inappropriate to investigate each threat very thoroughly before deciding how to act. It is better to act on a very small amount of information, and if in doubt to err on the side of safety. This implies that the decision rules should take a very simple form. This in turn allows the implementation of the rules to be ‘delegated’ to subconscious reflex-type activities.

It may be objected, at this stage of the argument, that because these simple rules are biologically programmed, they are not the subject of rational choice. It requires a ‘behavioural’ approach to explain them, it may be said. There is a simple answer to this objection, however. It hinges on the instrumental value of the rational action approach in generating testable predictions, which was alluded to earlier. By assuming that the human body behaves as though it had been designed to cope with short-term threats to survival, it is possible to predict quite successfully the sort of feedback control mechanisms that it possesses. This is more than a behavioural theory can do. A behavioural theory merely describes the