

Greg Davidson  
and Paul Davidson

# ECONOMICS FOR A CIVILIZED SOCIETY

'This remarkably informative,  
wide-reaching book is the  
civilized product of two civilized  
authors.'

**John Kenneth Galbraith**



**Second (Revised) Edition**

# **Economics for a Civilized Society**

**Second (Revised) Edition**

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To Louise and Tamah, and of course  
Arik, Gavi, and Zakkai



# Preface to the First Edition

How did we come to write *Economics for a Civilized Society*? In many ways we have been working on this book for years, in our learning, teaching and writings. In our careers as a Professor at Pennsylvania, Rutgers and Tennessee, and as a student at Swarthmore and Harvard, we have frequently seen the intellectual history of economic thought fall to waste as it is distorted to fit within the current conventional wisdom known as 'neoclassical economics'.

At one extreme of neoclassical economics is the intellectual despotism of a discipline which is more ideological than empirical. More commonly we have found intelligent and well-intentioned economists whose work is needlessly constrained and ruined by the weakness of these neoclassical conceptual foundations upon which they have built their analysis. Ours is not the cynical message that economists do not know anything – the problems we see come more from the things that economists 'know' that just are not so.

Our goal is to provide a civilized approach to the important economic policy issues that face modern societies. Unfortunately, conventional neoclassical economic thought cannot penetrate the operations of an enlightened society. Yet Western societies have invested a great deal of intellectual effort in developing the database and analytical tools of this conventional analytical analysis. Hence we have tried to salvage what can be used, if properly modified for a civilized setting, of the conventional wisdom.

We therefore provide a civilized analytical structure which can support work already done in neoclassical economics, when the latter is modified to integrate valid critiques of the conventional wisdom. In so doing we hope not only to improve our understanding of the orthodox approach, but also to probe the crucial interactions between the self-interest basis of neoclassical economics and the civic values to which the orthodox approach is blind.

An understanding of the boundaries of conventional analysis and how one can go beyond this restrictive barbaric approach is not merely of academic importance. Whether we like it or not, current economic theory has become the bedrock of our public policy decision-making process as well as the basis for our philosophy of society and its laws. Economic theory not only affects our bank accounts, but it also, in large part, determines how our society is fed and housed, and even how much we think our society can afford to defend ourselves against epidemics or enemies



threatening the very viability of our population. Conventional economic theory does influence our views of right and wrong, and can thereby change the context of our lives. Our hope is to provide guidance towards a more civilized approach to all these issues.

We would like to thank the following people for their comments on aspects of this manuscript: John Kenneth Galbraith, Robert Reich, Martin Kessler, Fred Zimmerman, Stephen Benko, William Kushner, Alan Plumley, Ellen Freeberg, John Powell, and Ellie Prockop. Others who have helped us with their comments on earlier aspects of what became the basis of this book include Amitai Etzioni, James Verdier, George Brockway, Dotty Robyn, Marty Linsky, John Dunlop, Malcolm Salter, Steve Kelman, Richard Zeckhauser, David Ellwood, Harvey Liebenstein, Shah Ashiqazziman, Peter Swiderski, Ken Sharpe, and Charles Gilbert. Not everyone mentioned above will agree with all of our findings but we appreciate the insights that their comments provided.

We would also like to express our appreciation to the late Sidney Weintraub who taught us, in separate economics courses almost thirty years apart, the importance of the statement of William Stanley Jevons that 'In matters of philosophy and science authority has been the great opponent of truth. A despotic calm is usually the triumph of error. In the republic of the sciences sedition and even anarchy are beneficial in the long run to the greatest happiness of the greatest number.' From Sidney Weintraub we learned much – but especially we learned that, although it is more pleasant and easy to agree than disagree, it is necessary to speak out against the fallacies which find their way into the conventional wisdom.

Finally, we wish to thank Louise and Tamah, whose contributions (editorial and other) would have earned them mention above, except that they also deserve special recognition for tolerating us as we frequently woke up at three in the morning to write down 'just one more idea'.

*Washington, DC*  
*Knoxville, Tennessee*

GREG DAVIDSON  
PAUL DAVIDSON

# Preface to the Second Edition

We have completely revised our book *Economics for a Civilized Society*. It has been eight years since we wrote the original version, and in that time we have seen a continuation of the erosion of civilized institutions of the Western World. In the interim more facts that support our earlier analysis have emerged and are incorporated in our discussion.

Politician of both major parties in the United States and in the United Kingdom argue that they want to provide a legislative economic programme to promote a 'civil society' that emphasizes the importance of values of the family and the community. Unfortunately, today political decision makers are trapped by the rhetoric of conservative economics that focuses so strongly on market values that it derogates family and community values. In *Economics for a Civilized Society*, we explore how we arrived at such a sorry state and by studying history we learn how we can again develop a prosperous and civilized global economy by developing civil principles that coordinate market values and civil values.

These past eight years have also seen many nations of the world throw off the authoritarian rule of communism and begin to experiment with free markets and democracy. The post-Cold War era has nations of the former East and West coming from opposite directions towards the same questions regarding the fundamental nature of their society. The internal debate over the proper role for government and for free markets is a crucial one, and it raises questions that can not be adequately addressed using conventional approaches to economics.

We believe that *Economics for a Civilized Society* can provide the foundation principles that will permit all nations to develop a role for their government that provides their citizens with a prosperous civil society operating within a global civilized community of nations.

Knoxville  
Tennessee

GREG DAVIDSON  
PAUL DAVIDSON



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# 1 In Pursuit of Civilization

A conservative philosophy of economics has dominated the political agenda of the 1980s and 1990s. This philosophy can be epitomized in the following question: What's the difference between love and prostitution? If we asked this question of those whose economic philosophy shaped American politics in the 1980s and 1990s, the answer is that prostitution is a valuable service that some people are willing to pay for, while love is not for sale and therefore is worthless. This philosophy of market valuations provides the basis for all values in conservative economics.

Conservative economics focuses exclusively on one of the two major types of human motivation: self-interest. Unfortunately the other source of human inspiration – what we refer to as civic values – is locked out of the conservative economic framework. Consequently, when debating national policy we can compare the costs and benefits of prostitution, but are blind to the importance of love.

Nations are built on the motivating forces of both self-interest and civic values. When self-interest and civic values are combined, they reinforce each other so that a nation can enjoy both prosperity and justice. Difficulties arise when society is governed by only one of these two forces because you can't buy justice in the marketplace, and similarly, you can't build prosperity on civic pride alone. A prosperous civil society combines self-interest and civic values so that the citizens may reap the benefits of each.

Unfortunately, in the last twenty-five years, we have come to view the nation's future in terms of choices between these competing parts of our heritage; self-interest *or* civic values. Liberals and Conservatives have each adopted a fragment of the national heritage as the centrepiece for their economic policies; social values for liberals and 'the bottom line' of self-interest for conservatives. As the political pendulum has swung, the policy choices that the nation has offered have, at best, provided improvements in one sphere at dreadful costs in the other. The liberalism of the Great Society programmes of the 1960s sapped the incentives behind the profit motive, just as the politics of self-interest in the 1980s and 1990s eroded and degraded civic values.

Unemployment and inflation are both evils. To deny jobs and income to those who want to work, that is, to *promote* unemployment in order to combat inflation, violates basic civilized values. To permit inflation, on the other hand, undermines the wealth earned by individuals acting in



accordance with their own self-interest. Liberals see the civic need for a fully employed society, even if this causes inflation and thus devalues the accumulated assets held by the wealthy. Conservatives, on the other hand, demand that inflation be stopped, even if this means that some people lose jobs and businesses lose profits as a result.

For more than two decades, the tragedy of economic policy has been the conventional wisdom that it is necessary to create sufficient unemployment to constrain inflation. The power of the anti-inflation (or pro-unemployment) philosophy was demonstrated as recently as early 1994. Policy makers at the Federal Reserve decided that inflation was a major threat since unemployment declined to 8.5 million workers (or 6.5 per cent of the labour force) in February 1994 from 9.4 million workers (or 7.4 per cent of the labour force) in 1992. These Federal Reserve policy makers (including two Clinton appointees) believed that it was more important to depress the growing economic prosperity to fight inflation than it was to continue growth in profits and jobs. The Federal Reserve raised interest rates to slow growth and reduce economic opportunities for the unemployed *who earnestly wanted to work*. This conservative approach is based on a false premise – namely that it is impossible to maintain a prosperous full employment society that is also protected from inflation.

## A NATURAL RATE OF UNEMPLOYMENT?

The view that a free market society requires a significant portion of its population who want to work to remain unemployed has its origin in the Marxian notion of the need for an ‘industrial reserve army of the unemployed’ to keep workers in their place. In its recent conservative manifestation this industrial army of the unemployed has been resurrected by conservative economists under the less-emotive appellation of the ‘natural rate of unemployment’.<sup>1</sup>

The concept of a natural rate of unemployment provides justification for Federal Reserve Policies that raise interest rates and encourages our government to move towards a balanced budget before full employment is achieved. Those who champion this natural rate concept are essentially claiming that it is bad for our society if businessmen hire more unemployed workers when market conditions provide profit opportunities for producing more output. This natural unemployment rate argument states that, by reducing the ranks of the remaining unemployed in response to possible profit opportunities, these self-interested businessmen will cause the economy to ‘overheat’.