SELECTED NOTES FROM CHAPTER TWO

Why Economists Disagree

Economists try to do what all scientists do – observe certain aspects of the natural or social world, gather data to measure those aspects, construct theories to explain the data, and test the theories against reality to validate or invalidate them. On the whole, however, economists do a weak job at all this. They commonly spend vast amounts of time observing each other’s articles rather than reality. Their data are poor, and they devote little time to improving them. Their theories are rigid and mechanistic. And they rarely discard them unless some academic or government position is at stake.

Is Economics a Science?

Yet the weakness of economics as a science isn’t entirely the fault of the economists. The reality they are trying to analyze and predict doesn’t lend itself to orderly and closed systems of analysis like, say, physics. The physicist can exclude “outside” disturbances, such as national elections or wars, from the particular system of atoms he is studying. The economist can’t really exclude anything that affects the economic system. His system is “open” – open to the storms of political, social, technological, psychological, and even climatic change. Not being able to predict all such changes, his powers to forecast the economy are weak. His very perception of reality is weak; his seemingly hard and precise numbers are soft, synthetic, inaccurate reflections of underlying events and moods and tendencies. One worthwhile reform of economic statistics
might be to outlaw the decimal point.

The problem of achieving scientific objectivity is worsened for the economist by his conscious or unconscious political and social biases and values. Is he a Republican or a Democrat, a disciple of Smith or Marx or Jesus or Ayn Rand? Does he identify with the rich, the poor or the middle class? Is he an elitist or a populist?

Does he believe that political freedom depends on preserving economic freedom and that economic freedom is achievable only under capitalism? Or does he believe that the great corporations of mature capitalist societies tend to abridge both political and economic freedom?

Does he conceive of society as a continuous struggle among classes, with the state the instrument of the dominant class, or does he see democratic society as one in which the state can and often does serve some general public interest?

All such questions are not just scientific; they are political, philosophical, and ethical questions as well.

It would help if economists made their political and social values explicit, rather than pretending to a spurious scientism. Unfortunately, concealed biases and interested political or economic motives commonly corrupt both economic analysis and policy.

Is Economics Propaganda?

The struggle for an objective economics has been going on for a long time. Back in the days before Adam Smith, in the sixteenth, seventeenth, and eighteenth centuries, the first economists were businessmen – international traders and merchants, known as “mercantilists” in the economic literature. Their economics was a form of special pleading for their own interests; they identified those interests passionately with those of the nation – as businessmen have tended
to do ever since. “What’s good for the nation is good for General Motors, and vice versa,” said
“Engine Charlie” Wilson. In 1621, Thomas Mun, a manager of the East India Company, put the
thought somewhat differently: “The nation is like a big family.”

What was good for one, said the mercantilists, was good for all. As it was good for a
merchant to amass riches, so was it for the nation. So the nation should save more than it spent,
sell more than it bought. If it did so, gold would flow in to balance the nation’s accounts. A
“favorable” (surplus) balance of trade was the road to wealth for the nation.

England and other nations, pursuing the mercantilist philosophy, tried to acquire wealth
by keeping out foreign goods – by taxing imports heavily and granting monopolies to their own
ships. The net effect of these efforts on every nation’s part to run a surplus (which is obviously
impossible for all) was to diminish trade and make individual nations poorer not richer.

Adam Smith’s Beneficent System of the World

Modern economics was born in Adam Smith’s effort to refute the mercantilists. He built
a system of thought to demonstrate how a nation’s interests – and all nation’s interests – would
best be served by the free flow of trade within an interdependent world economic system,
whether an individual company’s or industry’s immediate interests were hurt or not.

Unlike the mercantilists, Smith was no businessman but an academic, a professor of
moral philosophy at the University of Edinburgh. Like many of his contemporaries, Smith
worked under the influence of two great Englishmen who had preceded him by a generation – Sir
Isaac Newton, the physicist, and John Locke, the philosopher.

Newton’s *Principia Mathematica* had described the physical universe as a precise
machine, powered by a few simple forces; after Newton, scholars sought to find the same kind of
order in human beings and in human society. The human body, with its delicate network of nerves, muscles, glands, organs, worked marvelously well without apparent human will or direction. Societies of animals and insects constituted organic systems. Could not human society be the same? A Scottish philosopher, Thomas Reid, compared human society to a bee colony. While constructing a honeycomb of perfect hexagons, bees did not first set out to solve the geometry of the hive; each bee built without knowing what he was doing in relation to all other bees. Similarly, Reid argued, man did not know the ultimate purposes of his actions. He was guided by immediate impulses and emotions which somehow fit into a large plan.

Another philosopher, Bernard de Mandeville, shocked the respectable Adam Smith by arguing that private vices might be public virtues. Mandeville’s didactic poem “The Fable of the Bees or Private Vices, Public Benefits” sought to show that social benefits might flow from individual actions that might be regarded as morally objectionable; thus he praised spending (which created work for others) and deplored saving (which dried up trade). Mandeville even celebrated the social utility of sexual passion, whatever the purposes of the lovers; “I much question whether the civilized pair, in the most chaste of their embraces, ever acted from the care of their species, as an active principle.” This may have disturbed the respectable Smith, but it was close to his own ideas. In *The Theory of Moral Sentiments*, which preceded his famous *Wealth of Nations* by seventeen years, Smith wrote that we control ourselves and feel sympathy for others not out of any overwhelming love of mankind, but rather to satisfy our own most important desires – to be loved and to be cared for. The result is that, in trying to gratify ourselves, we individuals unwittingly benefit society.

Smith blended this rather weak defense of self-interest with the strong ideas of Locke on
the natural rights of man. Government ruled only by the consent of the governed, and its power must be carefully limited to serving the public interest. It was the individual who really mattered; the Lockean idea that every person had an inherent right to “life, liberty, and the pursuit of happiness” – as Thomas Jefferson phrased the principle – lay at the heart of both the American political revolution and Smith’s economic revolution. Smith’s great work of 1776 – its full title was An Inquiry into the Nature and Causes of the Wealth of Nations – united Newtonian order and Lockean freedom through the concept of an economy built on free markets, free trade, and the pursuit of self-interest. The desire to better our own condition “comes with us from the womb and never leaves us till we go into the grave. . . . It is not from the benevolence of the butcher, the brewer or the baker that we expect our dinner, but from their regard to their own self-interest. We address ourselves, not to their humanity, but to their self-love!”

Yet Smith was no Utopian who believed that the free market provided the solution to every social problem. Often his own best critic, he anticipated many of the injustices of the market that later economists would stress. He warned against capitalist greed and monopolies. He saw the danger that the division of labor in factories would breed intense boredom and what Karl Marx would later call “alienation” among the workers. Smith urged that the growth of industry be paralleled by a growth in education, to keep the worker from being turned into a “brute animal.” And he forecast the rise of the bourgeoisie – and the new class antagonisms that would result.

But Smith, child of the Enlightenment, remained an optimist; the Invisible Hand – that most powerful of all his metaphors, and perhaps the strongest in all of economics – would reconcile human conflicts and guide mankind to a happy end, if the state, that monster of the
eighteenth century liberals, did not interfere.

**Karl Marx Says Capitalism Is Doomed**

The most famous apostate from classical economics, Karl Marx, sought a radical change in the way society was organized. He appreciated the fantastic changes that the capitalist system had brought about – especially its productive power – but nevertheless thought the system was doomed by historical processes. The riddle Marx posed was: “What is to take the place of capitalism once the historical conditions that gave rise to it no longer exist?” That question shook the world – and is still shaking it.

Who was Marx? A lonely German intellectual without an academic post, a convert to Christianity from Judaism, a poor free-lance journalist, a son of the middle class who had married an aristocrat, a passionate revolutionary, he was at the same time a genius, one of those rare figures who transform the world.

A Prussian by birth and education, he left the country when his radical newspaper was shut down by the government. He first settled in Paris, later stayed in Brussels until he was expelled in 1848; he moved briefly back to Germany, to publish a radical newspaper. But in 1848, the year of *The Communist Manifesto*, the French and Prussian police, working together, had Marx expelled from the Continent. He fled to liberal England, the foremost capitalist power of the time.

Soon afterward, a Prussian policy spy wrote a description of the slum tenement in Dean Street, Soho, where Marx was living with his wife and three children and their (usually unpaid) servant: “He lives in one of the worst and cheapest neighborhoods in London. He occupies two rooms. There is not one clean or decent piece of furniture in either room, everything is broken,
tattered and torn, with thick dust over everything and the greatest untidiness everywhere. In the middle of the parlor there is a large old-fashioned table covered with oilcloth. On it manuscripts, books, and newspapers lie beside the children’s toys, bits and pieces from his wife’s sewing basket, cups with broken rims, dirty spoons, knives, and forks, lamps, an inkwell, tumblers, some Dutch clay pipes, tobacco ash – all piled up on the same table.”

On that very table was born Das Kapital – and, in a sense, the Russian and Chinese revolutions. Such is the power of ideas – when joined to the right historical conditions!

Marx used the classical economics against itself. He found nothing divine about the market, no Invisible Hand to guide it toward the greater good of all mankind. A market was simply a social arrangement that men had created – especially those men who stood to profit from the market – and that other men could, and would, in time destroy, when they decided that the market had outlived its usefulness or necessity.

The creed of self-interest, nurtured in the marketplace, could not be regarded as an eternal verity. Marx complained that Smith and his followers had looked only at one historical moment in time and thought they had discovered laws that would be good for all time. It was wrong, he said, for Smith to argue that man always functioned best when he operated according to his self-interest. This may have been true among the class of small capitalists at the end of the eighteenth century, but it certainly was not true in feudal or mercantile states where exchange was dependent on personal loyalties and other noneconomic relationships. Marx admitted that classical economists had gone far in understanding the market, but said that their “laws” of economic behavior were subsumed by a much greater economic relationship, one that existed in every society – that linking the producer to his product. In effect, said Marx, the worker owned
what he created – but was cheated of it by “capitalism.”

He departed from his predecessors in economics by asking new questions. He wanted to know, not just *how the market worked*, but *how it came to exist in the first place*. He asked, not how to keep the market functioning, but what would replace it.

He had no doubt that the capitalist system was “out of control” and that the market had, like Frankenstein’s monster, taken on a life of its own that made prisoners not only of workers but of the entire society. People no longer fulfill themselves in their work, said Marx, but deny their own humanity. They experience misery, not well-being. They do not work to satisfy the need to create, but only to satisfy other needs, to acquire money and possessions.

Thus, said Marx, capitalism changes the whole purpose of community life. In a pre-industrial society, people banded together for protection, to exchange goods, for a whole sphere of communal reasons. But under capitalism, said Marx, the fabric of society is torn to shreds and individuals think only of themselves.

Man’s creative impulse, said Marx, is directed by the exigencies of “the system” away from, rather than toward, the community. The individual longs to establish his identity as something more than a statistic, a sale, a unit of labor. But he sees others, in a market society, as competing labor units or competing (and richer) consumers – not as friends but as things.

That was how Marx interpreted Smith’s doctrine of self-interest. For Marx, this was not man’s natural state but merely a reflection of the poverty of human relationships in a market society.
1. For a boiled-down version of Adam Smith’s great work, see *Selections from the Wealth of Nations*, George Stigler, ed. (Appleton-Century-Crofts, c1957). For further reading in the history of economic thought, see Robert L. Heilbroner, *The Worldly Philosophers*, and Joseph A. Schumpeter, *History of Economic Analysis*, both cited in “Suggestions for Further Reading,” below. The reader who has time and interest will find Smith’s classic *Wealth of Nations* both readable and fascinating in its details.

2. There are many editions of *The Communist Manifesto*; one is cited in the suggested readings below. The work hits like a sledge hammer. By comparison, Marx’s *Das Kapital (Capital)* is tough going.