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Toward a Political Psychology of Economics

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This paper explores the relationship between economics and the other social sciences and the implications for public policymaking. There are significant limitations inherent in applying the abstract and fragmentary conclusions of economics directly to public policy matters without first resynthesizing those conclusions to the larger body of knowledge about human behavior and social structure. The general problems of discreteness and abstraction in the analytic sciences are discussed, as well as the types of problems encountered when cross-disciplinary work is attempted. Several examples are given of economic prescriptions that are off the mark due to a failure to incorporate basic knowledge from other social sciences. Possible adaptations are laid out, including the use of "policy science" as a less analytic but more encompassing level of analysis relevant to policymaking in the complex and unfragmented world of real phenomena.

KEY WORDS: fragmentation of knowledge; synthesis of knowledge; economics; socio-economics; abstraction; types of sciences.

INTRODUCTION

Economics, long considered the queen of social sciences, has been much criticized recently. Most critics focus on internal difficulties: questionable theories (from Keynesian to supply-side), poor measurements [consumer price index (CPI), unemployment statistics, gross national product (GNP)], reliance on data collected for other purposes and not verified, and excessive preoccupation with mathematization (Allvine and Tarpley,

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1977). My concern here lies elsewhere – with the basic relationship between economics and other social sciences and the significance of this relationship for understanding economic phenomena. To chart this largely uncovered subject requires drawing on the philosophy of science. This, in turn, I suggest, leads to both new theoretical insights and new practical foundations for economic policymaking.

At issue is the level of abstraction from the observed phenomena, the need for resynthesis, the limited ability to provide it, and the opportunity policy sciences offer as a supplementary synthesis. These points are next covered one at a time.

FIRST, YOU FRAGMENT

All analysis, especially all scientific analysis, proceeds by fragmenting the phenomenon under study. Instead of seeking to absorb or deal with a phenomenon in its totality, most observed qualities are deliberately and systematically neglected in favor of focusing on some others. A chemist may focus on the process of photosynthesis of a flower; a geneticist – on its chromosomes; an economist – on its price; a social psychologist – on the meaning of giving a flower. In contrast, a nonanalytic across-the-board approach of, for example, a typical photographer may try to deal with the flower as it is, in its entirety, without isolating any specific features. (Complete precision would suggest that these approaches also abstract and interpret – but to a much lesser extent, and are less conscious and less systematic about the elements they include versus the elements they neglect.)

While the fragmentation and abstraction that analysis inevitably entails have often been recognized, the resulting chain of effects is much less studied and above all, its consequences are not systematically taken into account. The first result is the generation of knowledge in analytic disciplines which parallels the fragmentation lines. Analytic systems or theories are constructed by grouping variables of one kind, either chemical *or* genetic *or* economic, etc. Propositions are derived within these segregated frameworks and are compared to data organized within these same categorical confines. Knowledge is accumulated and transmitted within these frameworks. We construct analytic towers and store knowledge in them.

THE LIMITS OF RESYNTHESIS

The knowledge accumulated in such fashion is highly analytic. Applying it, that is, understanding and predicting developments within the world of phenomena, works well as long as there are relatively few variables, all

members of the same analytic subset (e.g., all of physics *or* biology *or* chemistry, etc.), *and* the phenomena are segregated from all others, for example, the movement of the planets or the decay of radioactive material.

However, the more complex the set of variables involved, the less segregated the phenomena and the lower the ability to return from an analytic discipline to the phenomena. This is especially the case with living organisms, personalities, and social systems. Here it is often impossible to move soundly from conclusions about the relationships among variables within an analytic discipline to predictions about the phenomena under study.

The world of phenomena is simultaneously under the power of factors characterized by variables farmed out to other analytic disciplines. This point is highlighted when scientists reject the demand that their theories be tested by predicting future events. They properly hold that they can predict future "readings," "scores," or "values" of dependent variables, members of their theory, on the assumption that "all other things are held constant." It is freely acknowledged that in many situations such constancy cannot be realistically assumed; other factors change and impinge on the outcome. Then, a test of a theory can be achieved by sorting out the changes in the dependent variables (or effects) due to changes in the independent variables (or causes) under study, from the effects of other causes not studied. This will help the science, but not advance the understanding of the general phenomena, nor help in predicting their future development because they are subject to all the forces, not merely those the particular science chose to focus on.

True, in some situations, application—the use of analytic knowledge to deal with the real world—is successfully achieved without resynthesis. This occurs either when the segment of the phenomena is highly segregated and subject to characterization by relatively few variables; when a high degree of precision is not sought (the "imprecision" is the variance accounted by the other factors); when the other variables characterizing the phenomena change slowly (e.g., basic personality), or are temporarily set or dormant (e.g., values), which allows greater prominence to a subset of variables, the focus of the application. However, in all but highly segregated segments, sooner or later these other factors are activated, and hence application without resynthesis is bound to lead to erroneous conclusions and policies.

The proper way to proceed is as easy to depict as it is difficult to traverse. The proper way is to *resynthesize* the finding of the analytic disciplines before one acts in the concrete world affected by factors characterized by the variables into which the world was divided. The *resynthesized* flower would contain all the relevant information bearing on the flower and the variables which account for changes in the observed data—and, above

all, the relationship among these variables, not only within one discipline but also across disciplines. For example, it would take into account that excessive plasmolysis of cellular fluids will result in wilting, changing the flower's symbolic connotation and decreasing its price.

The reason this road is not often traveled is a double one. First, complex phenomena require a Renaissance-like mind to encompass the variety of variables and to combine data about their status and their effects on each other. Merely combining data of two close disciplines, such as chemistry and biology, often proves quite taxing. All encompassing is typically overwhelming, and, without being encompassing, some relevant variables may be left out.

Second and more deeply, to construct the analytic towers, meta-assumptions are introduced about the nature of the world and the processes within it. These meta-assumptions are specific to each discipline, and often incompatible with those made by another. Thus, much of economic theory tends to assume that people are basically rational and will act to advance their own self-interest. In contrast, the main parts of psychology, sociology, and social anthropology assume people to be largely governed by such nonrational forces as values and sentiments. Physiology in turn tends to treat people without assuming either capacity, governed by the basic processes as animals, without a special cybernetic capacity. As a result, cross-disciplinary work, indeed communication, is very difficult and often unproductive. There is no satisfactory solution to this problem. The difficulty of resynthesis seems to be a price the analytic approach must pay.

IN ECONOMICS

We are now ready to apply the implications of this line of analysis to the condition of economics. There are of course a variety of economics; however, the one I focus on here is the one currently dominant in the United States.² It is modeled after physics, to be (a) highly analytic (its concepts are highly removed from observable data; e.g., a distinction is made between "core"—or "underlying"—inflation and overall inflation, while the only inflation people experience is higher prices, which encompass both the hard and the soft core). (b) Relationships among variables are often mathematically expressed. (c) Meta-assumptions about the world and its processes are built into the theory (e.g., people supposedly would not work at a highly

²Other economics are referred to by adding an adjective such as classical, or institutional, or political, or Marxist.

hazardous job unless the benefits were enough to justify the risks because people are assumed to follow self-interest).

The phenomena which economics often studies seem more complex than those physics typically deals with in the sense that more variables seem to be relevant; e.g., productivity or economic growth may be affected by scores of variables. (I should add that this statement has not been subjected yet to a comparative, cross-disciplinary variable count). The segregation of economic factors from others is limited. *As a result, the direct application to "economic" phenomena of conclusions based on knowledge about relationships among the variables which economics encompasses is bound to fail*—because it neither resynthesizes (takes into account the other operative factors and the body of knowledge about them), nor segregates the subset tightly.

A brief example may serve. Economics assumes higher prices for a product will reduce the quantity demanded, because such prices bring supply and demand to "balance" at a lower volume of the product involved. This is in line with a piece of sociological data. People were asked, "generally speaking, do you think now is a good time or a bad time to buy (major) household items?" They were also asked if they expected prices to go up, "on the average, during the next twelve months." For a long time, most people thought it was not a good time to buy when inflation was on the rise—it seems they were expecting it to be temporary.

However, in 1977, their view changed drastically, with nearly twice as many (two-thirds) thinking it's a good time to buy now (versus one-third in mid-1974), despite a much higher proportion who expected prices to be higher. *Now* they seemed to be expecting inflation to be persistent (*Opinion Roundup*, 1978). Hence, rather than awaiting lower prices, they bought in the face of higher prices—seeing them as signals of still higher prices to come. (This new psychology of inflation has numerous implications for economic policy which need not detain us here.)

The preceding data illustrate the impact of changes in an "external" variable, expectations, on the relation between prices and quantity demanded. An economist might say that the change in expectations is one of those intangible factors that changed the overall demand curve, but that the relation between price and quantity demanded still holds, given the new demand curve.

However, this escape clause is really a tautology, because supply and demand are defined to always balance; the point is that, given all other assumptions economics uses to predict the adjustment of the curves, a change in expectations will make them intersect at a different point from that which the economist would have predicted.

Further, it raises the question of how to encompass the knowledge required to understand the dynamics of such a variable. It is relatively easy, at

least in the case at hand, to observe that the relevant external variable changed drastically. *However, this does not constitute an explanation of what accounts for the change.*

Why did most people not perceive inflation as persisting in 1974 but did so in 1977? One needs to answer this question, if one is to predict in the future when purchasing behavior might once again change course drastically, e.g., inflationary expectations subside, and use this information to fashion public policies.

For instance, when expectations are that inflation will persist, a recession induced by a tight monetary policy will produce much less inflationary relief and fall in interest rates than when no such beliefs are operating. Or, to put it differently, a deeper or longer recession may be "required" to have the same effects that in the previous environment were achieved by a lesser recession.

However, we do not know what turns expectation and these factors, not systematically synthesized, into *applications* of economics. An economist may say, quite properly, that economics cannot study "everything" and this other factor "belongs" to another social science. However, those who fashion economic policy must deal with such factors and concern themselves with their systematic relations to those variables economics does encompass.

SEVERAL ADAPTIVE MECHANISMS

Economists have responded to the difficulties presented by application without resynthesis with several positions and adaptive mechanisms. To reiterate, one approach is to suggest that the economists' duty is to deal with the variables their discipline encompasses. Resynthesis is not their business. This leaves the task of resynthesis to policymakers and other "actors" no more able to perform it than economists. And it makes all economic *policy*, i.e., suggestions for action in the real world, hazardous because it gambles that the external variables or constraints will remain constant. Indeed, several observers have chided economists for their willingness to move from economic theory to economic policy.

Some economists have taken the position that their "readings," predictions, and theories are "imperfect" but provide "first approximations." The implication is that while one does not deny the "existence" and consequence of other variables, nor that they have not been added in, their role is limited; most of the variance can be accounted for by economic factors. However, experience suggests that the models are *not imperfect but partial* and the approximations are not close enough to provide effective tools of policymaking.

A widely relied upon adaptation to action without resynthesis is after-the-fact correction (sometimes referred to as "mid-course" adjustment). The intervention was based on an economic theory; e.g., a 1981 supply-side tax cut, or a move to require higher reserves by the banks to slow the growth of the money supply in line with monetarist theory. The expected results were a higher level of economic activity *and* higher tax revenues (in the case of the tax cut) and a slower growth of money supply and less inflation (in the case of monetarism). When neither materialized by the end of 1981 as originally expected, various "new" factors, previously operative but not encompassed, were added to the framework (one or two at a time), and the policy was adjusted accordingly.

To use the example of monetarism, originally it was maintained that high interest rates would bring down inflation. When that didn't work, the rates were left to find their own level, and inflation was to be controlled by restraining the *size* of the money supply. When this too did not yield the expected results, monetarists changed the definition of the money supply that had to be controlled. And the very latest twist: money supply needed to be neither tight nor lax, but "regular," and future course "predictable," "steady," and "credible."

There is nothing "inappropriate" in these post hoc adjustments from a policy viewpoint. On the contrary, they constitute a realistic adaptation to the fact that many operative factors were previously ignored. However, from an analytic viewpoint, these post hoc adjustments, especially when they are introduced *not* as a systematic development of an improving theory but as ad hoc adjustments, are in effect a trial-and-error, "fishing," expedition. If this-and-that does not have quite the desired result, it "must be" this-and-that, or — something else.

In effect, in such a trial-and-error approach, all factors not cycled in are taken into account — but in unsystematic fashion. The larger the number of these factors, and the more variance they account for, the more uninformed the policy and the costs of the inevitable delays and zigzags. The aim of science is to reduce the range in which trial and error must be relied upon. I suggest that in dealing with the economic world, as distinct from science for science's sake, with *reliance on an analytic scheme without resynthesis* (or some substitute better than after-the-fact adjustments), trial and error plays too high a role.

In another "response" to the inability to resynthesize, economists have attempted to incorporate into their theory noneconomic factors, in effect trying to make economics coextensive with resynthesis. The main difficulties with resynthesis *within* economics are basically the same as attempts to resynthesize economics with other disciplines: the need for Renaissance-like minds and, above all, the incompatibility of meta-assumptions.

A particularly striking case is provided by the theory of rational expectations. As we noted above, statistical data suggest that people's expectations about the future course of inflation (will it subside or persist) affect their current behavior. This is easy to observe; however, to understand it, we must determine the underlying factors which change people's expectations about the future. Economists tend to account for these changes with the assumption that people behave rationally.

For example, according to one line of analysis, under Rational Expectations, past price changes largely determine expectations of future price changes. And there are some data to support this approach. For instance, between 1965 and 1969, "price movements in the month prior to the expression of expectations were found to be the primary 'cause' of expectations" (Katona, 1980). The consumer price index (CPI) correlated with the level of the index of consumer sentiments (ICS) at a high -0.76 (Katona, 1980).

However, in the following years other factors intruded, especially changes in people's trust in government, a *nonrational* factor (subject to emotional and symbolic factors). As a result, the correlation between CPI and ICS dropped to -0.65 (1970-1974) and then to -0.34 (1975-1979). While this cannot be demonstrated here, other attempts to use economics not merely as the queen of social sciences but as encompassing the social sciences, at least insofar as economic phenomena are concerned, have led to similarly unsatisfactory results. For instance, economists routinely suggest that the factors that drive productivity or economic growth (both areas in which economic variables and human motivation and institutions are closely intertwined) remain "largely a mystery."³

A more productive adaptation is to use policy sciences to supplement the use of an analytic discipline and in effect act as a surrogate resynthesis. Policy sciences are much less analytic than economics (or experimental psychology, or mathematical models of social or political behavior or of linguistics). Their terms (which define their variables) are closer to the observed phenomena than those of analytic disciplines. Their scope parallels the phenomena they encompass (e.g., medicine deals with the body, not a genetic or chemical slice of it). They draw on several analytic disciplines simultaneously (e.g., engineering draws on both thermodynamics and mechanics).

Most important, they organize and transmit large amounts of applied knowledge which has no analytic basis, but is of great applied policy relevance as a supplement *and* corrective to the analytic elements. In applied economics, for instance, the various analyses, which go into formulating

³Both Joe Pechman of the Brookings Institution and Herbert Stein of American Enterprise Institute have made this observation. See also Edward F. Denison.

seasonal adjustment of employment data and money supply data, have no theoretical basis but improve knowledge and policy.

Another noneconomic addition to economic theory, made by Herbert Simon, was the realization that humans and businesses cannot know what effects their decisions will have with any degree of certainty. Instead, people and firms try to set reasonable goals and to choose paths likely to lead to those goals. The result is that many actors' maximum good is not realized or even sought, and thus the economy is advanced less than classical theory would have it. A broader view, encompassing common sense and psychology, here supplements the economic model of behavior.

To build up the policy science of society, in particular the elements needed for dealing with the economy, it is necessary to revive and develop older traditions of political economics. This line of approach was never truly stopped. It continued under such labels as psychological economics (for instance, in the work of George Katona), developmental economics (e.g., Albert O. Hirschman, Gustav Ranis), institutional economics, and other such labels. But, for decades, it was considered a marginal approach while analytic economics reigned. The findings of these other economics (I'll refer to them in summary as "socioeconomics") were neither integrated as a rule into analytic economics nor used to supplement or correct the application of analytic economics to economic policy (Etzioni, 1980). Indeed, analytic economists tended to ignore these bodies of knowledge on the grounds that they were not quantitative, mathematically expressed, and analytic.

However, in recent years, the rising difficulties of analytic economics and its application have suggested that it is necessary to develop and draw upon socioeconomics aside from analytic economics. Socioeconomics will encompass knowledge relevant to understanding and dealing with economic phenomena, gleaned from social science disciplines other than economics, and distillation of experience and observation of resynthesis without analytic foundation, just as medicine draws upon chemistry, biology, and psychology, in conjunction with distillation of experience and observation of resynthesis.

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