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A better way?

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As neo-classical economic theories face severe criticism for their unreality, new approaches are emerging

Neo-classical economists, members of the dominant school of economics in the west, have an iron-clad response to all the criticism levelled at them: Show me a better way! While many criticisms of neo-classical economics are at least 200 years old, the barrage of criticism has intensified in the last decade as western economies suffered from low growth rates, high unemployment *and* high inflation.

Excessive preoccupation with mathematical virtuosity further alienated most who once followed or tried to apply neo-classical economics. When I recently expressed surprise that Modigliani gained a Nobel Prize for his life-cycle saving theory, a theory incompatible with the facts, an economist responded: "In economics it does not matter if you are right or wrong but how elegantly you do it." A recent Harvard graduate, teaching labour economics, confided: "I don't believe a word I am teaching." MIT economist, Lester Thurow, who unleashed one more barrage of criticism in his 1983 *Dangerous currents*, called, like many before him, for the re-integration of economics and its sister social sciences as the way to overcome the unreality of neo-classical economics.

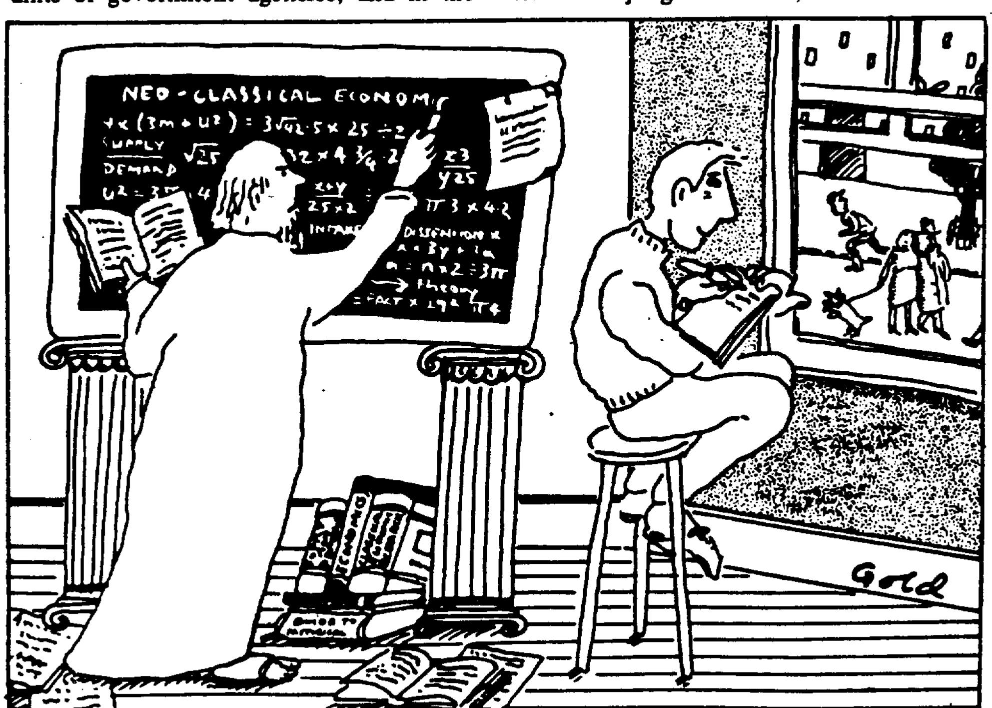
This is now beginning to happen. A large variety of groups on campuses, in research units of government agencies, and in the so-called think-tanks, are trying to form new approaches. These include various neo-Marxist endeavours, a Catholic group (centred around the *Review of Social Economics*), a humanist-psychology effort, and a liberal group (*Journal of Post-Keynesian Economics*.)

Most efforts, though, are less self-conscious about their value-assumptions and more concerned with following the traditional academic rules of the game. These efforts include groups interested in behavioural economics, which combines psychology and economics (two new journals: *Journal of Economic Psychology* and *The Journal of Economic Behaviour)* and the Society for the Advancement of Behavioural Economics (which will hold its next international meeting in Israel). Another group meets annually at Middlebury College in Vermont. On the sociological-economic front, in the USA, interesting work is being done on the west coast by Neil Smelser; in the mid-west by James Coleman and Arthur Stinchcombe, and in the east by Rosabeth Kanter and by Mark Grannovetter. The British Sociological Association is planning a new journal, *Work, Employment and Society*. Similar efforts are underway in numerous other countries.

While all these bubbling efforts are a long way from providing an alternative paradigm to neo-classical economics, they implicitly share a set of assumptions, pointing to a joint minimal platform. Its elements are briefly as follows:

- Instead of accepting the utilitarian notion that individuals are driven by pleasure, profit or self-interest, the new approaches assume that people are motivated by a wide variety of objectives, including service to others and to the community. Many seem to accept the basic notion that people, unlike animals, can judge their preferences and do not automatically yield to them. The moral valuations of where one's urges are pointing are the main criteria of judgment. Thus, while one's first impulse may be to do away with a particularly effective competitor, the taboo against the use of violence leads, instead, say, to the re-doubling of one's efforts.
- Instead of assuming that individuals are rational, their choices are assumed to be largely the result of habit or governed by emotions ranging from outbreaks of impulses to a desire to protect one's self-esteem. To the extent that decisions are based on knowledge, a vast array of recent experiments have shown beyond reasonable doubt that individual cognitive capabilities are not merely much more limited than neo-classical economics assumes, but also lead individuals to systematic biases in their decisions. Millions of people pay stockbrokers, even though their advice, on average, does not improve one's investment. Numerous consumers buy very expensive life insurance which yields little, while inexpensive and better term insurance policies are available. Many keep money in low yield savings accounts and borrow money at high cost from their bank or on their credit cards. In short, it seems that to assume not only an emotional but also an *incompetent* decision maker as a starting point is much more realistic than the opposite assumption.
- Free-standing individuals are not the main originators of decisions in economic or other matters. The main decision makers are individuals who are members of groups, affected by peer pressures and group leaders. For example, people by and large follow the trends of the groups to which they hail. Thus, recently in America, especially among college-educated groups, drinking to excess is no longer considered "macho" but unhealthy and dangerous. This is the result not of millions of individuals having reached that conclusion on their own but of the influence of a new temperance movement, led by Mothers Against Drunk Drivers, as well as by a national fitness and health craze.
- The economy is viewed not as a free-standing "market" but as nestled within a society, guided by its political processes and its culture. Hence to understand the behaviour of large corporations, labour unions, consumer associations and so on, one must study not merely their economic exchanges but also their relations to the body politic and their cultural standing. For example, it makes little sense to see the farmers as a highly competitive bunch because many have small lots and hence cannot "control the market" as economists tend to do; one must take into account that they form political organisations which intervene in the market, and that this lobby benefits from a nostalgic view of what farms used to be.

All this is still very sketchy, and there are almost as many disagreements among socio-economists as there are between them and neo-classical economists. However, socio-economics has moved beyond the stage of merely taking pot shots at neo-classical economics; there is a ground swell of endeavours seeking an alternative paradigm.



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