

Ideologues, Counsellors of the Prince and Participant Observers. Reflections on the Economics Profession

Paolo Ramazzotti
ramazzotti@unimc.it

1. Introduction

Are economists in any way responsible for the present economic and social situation? I think we should distinguish different types of economists according to how they address a more specific question: is a positive change in people's lives desirable and possible? Once we consider those who provide a positive answer, a further distinction is what they believe such a change can consist of and how it can come about?

Despite the apparent simplicity of these questions, the degree of specialization in the profession is such that how to treat them may not be evident in a great deal of research. Indeed, the richness of theoretical insights that different strands of thought lead to may suggest that it is not possible to make such distinctions.

While theoretical richness is important, it is nonetheless the case that, when decisions concerning public policy are concerned, economists must provide concrete answers. How they do so is often a much simpler matter than the diversity in their theoretical stances would suggest. Most often, the issues raised relate to some combination of efficiency and social justice. Obviously, these concepts must be adequately defined but this is precisely what makes it possible to distinguish the different strands of thought.

My basic argument in what follows is that, if we care to answer the questions above, what is at issue is less the availability of new analytical techniques – however important these may be – than the general view of the world and, consequently, the “mode of thought” (Dow 1996, 2008) that the economist has. More specifically, I will distinguish economists in terms of how they believe the economy is coordinated. In this perspective, I will consider two major strands of thought. One considers that coordination is based on relative prices, however complemented by institutions. The other considers that other circumstances, completely independent of prices, are also important.

A reasonable way to address the discussion would be to distinguish orthodox, or mainstream, from heterodox approaches. The problem is that the meaning of these terms is open to debate. The paper, therefore, begins with a brief discussion, in Section 2, of how these concepts have been dealt with in recent research. It points out that the accounts provided may well be insightful but do not help us to adequately discuss the basic question this paper wishes to address. Section 3 outlines the key features of the first approach, the price-centered one. Section 4 argues that price-centered coordination is not inconsistent with an evolutionary understanding of the economy. Section 5 points out how institutions and knowledge fit into this framework. It stresses that the latter remains an open issue, which either involves a very restrictive view of the world or an inadequate discussion of change. Section 6 presents the second approach by discussing prices as part of an instituted economy, thereby assuming that the former can exist only insofar as the structure of the economy is preliminarily determined. Section 7 elaborates on this issue by stressing that what underlies the distinction between the two approaches is their view of systemic openness/closure. Section 8 provides an exemplification of how the two approaches address concrete issues by presenting a brief discussion of a historical case: the attempt by France's President Francois Mitterand to carry out an expansionary macroeconomic policy during the monetarist 1980s. Based on the preceding discussion, Section 9 points out that if open systems

economists underestimate the methodological differences between the two approaches, the risk is to do bad economics. Section 10 briefly concludes.

2. Is “mainstream” singular or plural?

The main question - whether it is possible to hold economists responsible, at least to some extent, for the present situation - has to be formulated in a detailed way. Economists are not all alike. The issue is how to distinguish and classify them.

The most common approach is to distinguish a neoclassical mainstream from heterodox approaches. This is not a very satisfactory distinction. It is of little use to include in a single heterodox group people who follow rather different approaches to economic thought. As for the mainstream, many economists may use neoclassical tools and concepts but acknowledge that the world definitely has little to do with a Walrasian general equilibrium of a perfectly competitive economy. It is most likely that, in their attempt to join their theoretical approach with an intellectually honest awareness of the real world, they are confronted with dramatic internal theoretical inconsistencies. It is doubtful that this should be a major problem. A great many issues remain unsolved in most – presumably all – strands of economic – and possibly non-economic – thought. This cannot deter students from focusing on only some of them, hoping that other scholars will be able to tackle the remaining ones.

An attempt to overcome the above distinction is in Colander, Holt and Rosser (2004¹) who distinguish between mainstream and orthodox approaches. They contend that “Mainstream consists of the ideas that are held by those individuals who are dominant in the leading academic institutions, organizations, and journals at any given time, especially the leading graduate research institutions.” (Colander, Holt, Rosser 2004: 5). Non-mainstream economists include two groups of backward-looking people: those who are not up to date with cutting edge research, and heterodox economists. “The term heterodox [...] is usually defined in reference to orthodox, meaning to be ‘against orthodox’” (ibid.: 6). Orthodox, in turn, refers to a specification that “usually comes decades after the time period has existed. Thus, orthodox specifications inevitably are backward looking, not current or forward-looking.” (ibid.: 6). Viewed from this perspective, the only economists that can be truly considered responsible for anything are those of the mainstream. All other economists are simply missing the point, either because they are not informed or because they struggle against a fetish, a once dominant but now marginalized (by the mainstream) school of thought.

There are at least two problems with this reading of economic thought. First, while it explains how both the mainstream and heterodoxy relate to orthodoxy, it is not clear about how they relate to each other. Thus, if it is plausible that “by the time that the term [orthodoxy] becomes generally used, a large part of the mainstream profession disagrees with important dimensions of what is then thought of as orthodoxy”, it is not wholly clear why “heterodox economists refuse to work within the framework of mainstream economics”. It is obviously possible to claim that heterodox unacceptance of “the nature of the modeling process used, or the assumptions emphasized” by the mainstream depends on narrow-mindedness. It is nonetheless possible to argue that mainstream dominance may not coincide with an undisputable understanding of what is relevant: interesting and stimulating as the mainstream may be, other perspectives may provide insights that the mainstream fails to come to terms with. It may also be the case that the mainstream consists of relevant theoretical “bits and pieces” that, although intellectually

¹ A somewhat milder reassertion of their ideas is in Colander, Holt, Rosser (2007).

appealing, do not provide either a comprehensive understanding of how the economy works or appropriate guidelines for policy.

Second, and strictly related to this “bits and pieces” issue, a definition of the mainstream in terms of the professional success of its members does not warrant consistency among them. But if this is the case, that is, if the mainstream cannot be conceived of as a fairly consistent theory of how the economy works, any attempt to classify its different strands of thought must inevitably refer to some point of reference. It is, therefore, not surprising that Davis (2008) suggests a more detailed classification of economic thought which includes not only professional success but also distance from “fundamental assumptions at odds with neoclassical orthodoxy” (ibid.: 354).

Davis’ qualification provides for “an eight-fold classification of heterodox approaches” which suggests that heterodoxy is definitely more interesting than Colander et al. would have us believe. Much like the latter, however, he focuses on the novelty of “research programs” like “classical game theory, evolutionary game theory, behavioural game evolutionary economics, behavioural economics, experimental economics, neuroeconomics and agent-based complexity” (ibid.: 349). His concern is on how they relate to dominance in the field, thus how they may eventually lead to the emergence of a dominant approach. To this end, he draws “on extensive literature from the sociology of scientific knowledge” (ibid.: 351), which “argues that academic and professional disciplines recurringly structure themselves around dominant approaches on the grounds that this enables individuals within those fields to organise themselves in coherent (academic or professional) social groups, which then maintain themselves relative to similar (academic or professional) social groups that potentially lay claim to their research domains.” (ibid. 351-2).

This approach to dominance is helpful as long as the issue is the internal dynamics of the disciplines². It is less useful when the issue is how the research outcomes of the discipline relate to the “real world”: Davis’ whole inquiry holds independently of whether the discipline is completely self-referential or not. Indeed, while dominance is a quite understandable concept from a sociological perspective, it lacks a rigorous definition from the perspective of economic thought.

The research programs cited by Davis question a great deal of neoclassical assumptions but they do not provide a general interpretative framework of how the material reproduction of society is coordinated. They generally acknowledge that prices cannot be a unique coordinating instance but they stop short of providing an alternative, if incomplete, approach to coordination. Contrary to Keynes’ (1973) shift from a theory of relative real prices to a theory of a monetary production economy and contrary to Marx’s (1867) idea that prices are a byproduct of historically determined social relations of production, the above strands remain potentially, albeit not necessarily, consistent with a price-centered coordination of the economy such as the one theorized by neoclassical and Austrian scholars.

The above is less a critique than a qualification and a specification. It points to the need for a different type of classification of economic thought when the issue is not the direction taken by the discipline but the responsibilities economists have relative to how “real world” economies change and perform. Insightful as they may be, these approaches are not theories in the sense one uses the term with regard to neoclassical theory, i.e. as “the general or abstract principles of a body of fact, a science, or an art” (<https://www.merriam-webster.com/dictionary/theory>)³. In this perspective, they do not provide a framework to assess policy and policy suggestions coming from economists. Truly, neoclassical theory – in its various strands – may not fulfil such a task either but

² It also leads to interesting insights such as the one whereby specialization is leading to a dispersion among different strands of thought (Cedrini, Fontana 2017).

³ This is only one of the definitions of theory provided by the Webster’s on line dictionary. While Davis carefully avoids a confusing use of this term, it is often the case that reference to neoclassical *theory* and, say, transaction cost *theory* leads to the impression that these two “theories” are on the same standing.

it does provide a rationale for the price-centered coordination that many other economists in one way or other implicitly assume. The discussion that follows is based on the assumption that a major issue in economic thought has to do with the role prices have in the coordination of the economy and that a distinction between orthodoxy and heterodoxy may be formulated better by focusing on this issue. The section that follows will therefore outline the broadly neoclassical perspective on prices.

3. The market: a price-centered concept

Economic theory in standard textbooks is based on neoclassical microeconomics. The cornerstone of the theory is that prices are the main coordinating instance for all decisions that have to do with economic activity. The reason for this is that prices are claimed to transmit information concerning preferences and relative scarcity of resources. The main claim of this theory is that, provided some requirements are fulfilled, economic agents can choose in relation to prices alone. Consequently, in so far as possible, the price mechanism (the market) should be structured in such a way that prices can actually play their coordinating role.

A typical way to focus on the above assumptions is the structure-conduct-performance framework:

STRUCTURE → CONDUCT → PERFORMANCE

The ideal structure of the market is a perfectly competitive one. Agents adapt to the incentives and constraints that it provides. Their resulting (maximizing) conduct leads to the performance of the economy as a whole. Given the ideal structure, such a performance is a Pareto-efficient one.

The structure may fail to meet the requirements for perfect competition: market failures prevent prices from appropriately (efficiently) coordinating the choices of the agents. When this happens, agents adapt to prices that do not reflect actual preferences and scarcity. The resulting performance is inefficient.

The policy issue, under these circumstances, is whether and how to deal with such shortcomings. Given the causal link above, the best action would be to act on the structure of the market. Indeed, this is the solution sought by economists who, even when they do not adhere fully to neoclassical theory, are nonetheless confident in the coordinating potential of relative prices⁴. Sensible neoclassical economists, who look at how the world actually is, may acknowledge that some market failures cannot be removed, so that a Pareto-optimal performance is impossible. For instance, although assigning property rights in order to avoid externalities might appear to be an appropriate structural measure, its practical deployment may turn out to be rather complicated. An alternative might be to use taxes and subsidies to affect conduct, as with a Pigou tax. The enactment of such a measure, however, may be deemed too demanding – in terms of the required information and/or of its management cost – so that the best action may consist in merely making up for the undesired performance of the economy by changing – through taxes and subsidies – the outcome originally achieved, e.g. by compensating those that suffer the consequences of an externality. In turn, this may affect incentives, thereby leading to further failures. Ultimately, the problem is to choose the policy action that reduces the consequences of market failures as much as possible. Whether solutions pertain to structure, conduct or performance, the result is that some rule, or set of rules, is introduced that regulates prices so that they can coordinate the economy in the best of ways.

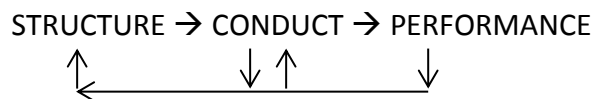
⁴ Buchanan (1991), Coase (1988), Ropke (1960), Vanberg (2001).

Even in the absence of market failures, a sensible economist may acknowledge that the separation of economic welfare from general welfare is conceptually useful but does not apply to the real world. Under these circumstances, a policy maker has to choose how to balance the efficiency of price coordination with extra-economic ends. The depiction of such ends depends on a value judgment that is independent of prices. The actual choice, in turn, involves a trade-off which is based on existing prices. Policy makers may, therefore, achieve a non-economic goal albeit by distorting coordination. Given these premises, the task of the economist is to understand the economy in order to point out how price-related constraints (trade-offs) affect the pursuit of policy goals.

4. Prices and evolution

Evolutionary developments in economic thought provide a different approach to economic policy. They acknowledge the existence of positive feedbacks which may lead to processes of cumulative causation that need not converge towards some equilibrium (Arthur 1999; Elsner, Heinrich, Schwardt 2015). This non-linear causation may lead to the emergence of a structure that, insofar as it is not the mere sum of the actions of single actors, is unpredictable. Furthermore, owing to the path dependence intrinsic in the positive feedback process (David 1997), the outcome of a given cumulative causation may be inferior – according to some predefined criterion – relative to that of other possible processes which were not enacted at the outset.

The implication for the structure-conduct-performance framework is one of interdependence among its components: performance affects both (market) structure and agents' conduct. Conduct, in turn, affects performance directly but also indirectly, through its feedback on structure.



A priori, with all three components changing according to some rule, any type of outcome is possible: convergence towards a fixed point, a periodic trajectory (e.g. some type of cycle) or a chaotic one. If these were the only features in evolutionary economics, the policy implication would simply be that one should take account of the above interaction. Insofar as a pattern of change can be modelled, policymakers would be able to act on parameters and achieve their goals.

This cybernetic view of policy is rather restrictive and scarcely convincing. First of all, it is generally acknowledged that economic actors are neither substantively rational nor perfectly informed. There are two ways to deal with this issue. The first one is to assume that agents behave in a maximizing way even though they are not equipped for such a task. New Institutional scholar like Williamson, for instance, believe that bounded rationality is not inconsistent with a “relatively” efficient outcome (Williamson 1993). The second approach is to follow Simon (1976) and to conceive of behavior in terms of a procedural rationality that pursues, and eventually leads to, a (merely) satisficing outcome. Either way, the above constraints on behavior imply that agents cannot take account of all possible information. Decisions formulated according to these behaviors will hardly achieve a Pareto-efficient general economic equilibrium.

A second acknowledgment is that economic agents do not merely adapt to existing constraints. They try to overcome them through a discovery process that, hopefully, will lead to an innovation. How the discovery process – and the trajectories and paradigms it leads to - occurs depends on what type of knowledge learning agents deem relevant: what they learn may involve a variety of

disciplines, e.g. those that have to do with technology, internal and external organization, finance, etc. It may lead to the introduction of technical changes but also to changes in how knowledge affects interaction, so as to align different perceptions of convenience and involve different actors in a business goal (Witt 1998): company culture and leadership as far as workers and companies within the value chain are concerned; marketing and advertisements for customers; lobbying for governments; advertisements and propaganda for the citizenship.

Learning - the discovery of what was previously unknown - implies that it is impossible, at least to some extent, to foresee the outcome of an evolutionary process. What is important, however, is to understand what criteria provide the guidelines for the learning process: more specifically, what makes the innovator decide what is relevant. For instance, although according to Schumpeter (1934) innovation may occur in different ways, its success is profitability as determined by relative prices. As we shall see, further on, other criteria are possible.

The above examples lead to a third issue that recent research emphasized: economic actors do not only interact with the anonymous signals coming from the market. They interact directly with other actors. As the examples here provided suggest, interaction occurs at two distinct levels: the “real” and the cognitive ones. For instance, a policymaker who wishes to prevent environmental pollution. She may choose to impose a Pigou tax on a polluting industry. Firms in that industry will react, at the real level, by reducing output. At the same time, at the cognitive level, they will try to find some way to make up for the profit loss that the tax implies. They may choose to seek some new non-polluting technology that will allow them to return to their previous output. Alternatively, they may seek some legal loophole to avoid paying the tax. In order to contrast the latter strategy, the policymaker may choose either to reinforce her top-down approach – e.g. through rigorous enforcement - or, alternatively, to change the nature of the problem by making it convenient for firms to pursue the collective good – clean environment – as if it were a private one: an example might be to arrange an R&D facility for the industry as a whole that will make it more convenient for firms to innovate (Elsner 2001; See also Elsner 2015).

Summing up, economic actors do not merely adapt to prices but they both interact directly among themselves and with policymakers and, in so doing, they learn. Policy makers, just as other actors, must therefore take interaction and learning into account. This is not the end of the story, however. When policy changes the structure of the economy, it is most likely that new opportunities, new incentives and new constraints will lead to possible changes in the strategies of the firms. Consequently, policymakers will need to revise their strategies as well. This broad evolutionary approach is compatible with conducts centered on prices as well as on other coordinating instances. We are, therefore, left with the question how these coordinating instances relate to each other. This is the topic of the next section.

5. Prices and institutions

Given how institutions are important in the economic discourse of many conventional economists, focusing on prices alone may give the impression of a straw man argument. The issue is where institutions come from. One conventional argument is that they are a (relatively efficient) solution to the shortcomings of the market. They are the rules of the game (North 1990) but the game remains the same: it is always centered on price-based choice. Alternatively, they are viewed as an (exogenous) circumstance that prevents prices from functioning properly so that they deter economic growth. Here too the assumption is that prices would function properly if only there were no impediments. Both views basically consider the economy a closed system with institutions either supporting this role or being an obstacle. Truly, some interaction exists with the

surrounding social environment (Williamson 1998), and the outcome may not be an ideal one⁵ but this does not prejudge the “relatively efficient” allocative function of prices.

The substantive frailty of this assumption should be rather straightforward. Interaction between the economy and the social environment is not a minor issue. Economic conditions affect the livelihood of people. When they cause dismal living conditions, this feeds back on mutual trust, on confidence in the “system” and on the cost of dispute management as well as of social unrest. Similarly, changes in the natural environment - that only few people fail to associate to economic causes – determine outright damage, droughts, famines and migrations that feed back on economic conditions. The interaction between the economy, on the one hand, and society and the natural environment, on the other, denies the systemic closure of the former.

Aside from these observations of the real world, let us look at the issue from a more abstract and formal perspective. The discussion above suggested that the absence of substantive rationality prejudices maximization and optimality, thereby precluding the informational function of prices, thus their effectiveness in coordination. In other terms, if prices are “wrong” they do not provide the information required to improve price coordination: for instance, you cannot assign property rights to achieve efficiency by measuring efficiency with inefficient prices (Ramazzotti 2012).

Another way to look at this issue is to consider an action that aims at significantly changing the economy. We are confronted with two possible outcomes: what would have been achieved with the pre-policy structure and what will result from the post-policy structure. These two outcomes – thus also their different patterns of evolution – can hardly be compared in terms of their prices. The economic structures that determine them have distinct sets of relative prices and distinct patterns of evolution⁶. In other terms, prices cannot be the assessment criterion for themselves. Consequently, existing institutions cannot be assessed in relation to how they act upon prices. Exclusive reliance on prices leads us nowhere in terms of a normative valuation.

As mentioned above, institutions may also be viewed as exogenous constraints. The relevant issue, here, is less that they may slow down adaptation to prices than that they may preclude it altogether: this is what underlies North’s (2005) concern with ideologies. It is an issue that takes us back to how learning and knowledge affect economic behavior.

While many authors acknowledge that economic actors learn in their attempt to improve upon the status quo, the issue is what and how they learn. According to Austrian and many Schumpeterian authors the guidelines of learning processes are provided by economic convenience as it results from relative prices (Hayek 1945, 1949). It is nonetheless the case that an Austrian like Hayek was forced to concede that learning processes need not be centered on prices. When he criticized “constructivism” (Hayek 1978) he implicitly acknowledged that learning is not bound by market conditions: people may seek goals that transcend market conditions. Hayek obviously believed that such a pretense was bound to preclude the appropriate functioning of the price system but, quite independently of this judgment, what is important is that he conceived of knowledge as an open system. Before we discuss the implications of this systemic openness let us look at some less conventional approaches to price-centered coordination.

6. Prices within an instituted process

⁵ Critique of alternative perspectives that are more prone to direct public action even turns to sarcasm when the latter are labeled “Nirvana approaches” (Demsetz 1969; see also Coase’s 1988) reference to “blackboard economics”. One might be willing to acknowledge the grain of truth there is in such critiques if the direction they point to did not boil down to a mere acceptance of the status quo.

⁶ A comparison would be possible in terms of physical quantities: given the heterogeneity of the outputs, their aggregation would require a standard commodity (Sraffa 1960), which confirms the claim that prices do not allow us to choose between different economies.

The discussion of neoclassical theory pointed out that its theoretical framework clearly separates the rules that regulate the economy from those that underlie society. The former are independent of the latter. Although society may choose to put its priorities before economic ones, this has a cost. Thus, policy may allow price-centered allocation to be more efficient but it may also pursue non-economic goals that are inconsistent with efficiency. In this case it will have to take into account a trade-off between economic and non-economic goals. The typical case is the efficiency-equity trade-off but other goals may well be envisaged, for instance in relation to the defense of civil or social rights.

Karl Polanyi (1944) pointed out the inconsistency of this closed systems view by stressing that, while a price-centered economy required prices to coordinate the production and use of commodities, the specific economy we live in – a capitalist market economy - cannot rely on commodities alone. Rather, it is based on two “fictitious” commodities: nature and labor power⁷. It could hardly exist without them although they are not proper commodities in that they are not produced according to relative prices.

This conceptual inconsistency reflects a real inconsistency that has dramatic human, social and societal consequences. By treating labor force and nature as plain commodities, a capitalist market economy causes the human and social costs of unemployment and of unacceptable living conditions as well as those of environmental disruption⁸. In so doing, Polanyi argues, it tends to undermine the basic values that hold a society together. It is these values that underlie what he refers to as a double movement: the attempt to subject price coordination to societal constraints.

Polanyi raises two important issues, here. First, the price-centered allocation rules that regulate a capitalist market economy also tend to regulate the society it is a part of. Second, the clash between the economy’s rules and societal values occurs because the latter are – at least to some extent - independent of the economy and operate in the opposite way: they tend to constrain the functioning of the price-centered economy. They are determined by a learning process that – contrary to what we saw with regard to innovation in Schumpeter - need not be guided or constrained by prices. Consequently, there is an interaction between economy and society that disproves the implicitly assumed systemic closure of the former.

Following Commons (1924), some institutionalist scholars (Bromley (1989), Samuels and Schmid (1997), Schmid (1987)) criticize the closed systems view of neoclassical theory from another perspective. They point out that markets cannot function unless they are organized by a legal system. Depending on which legal-economic nexus is established, different structures are possible, each one with its own potential efficiency. According to this view, rules such as a ban on child labor operate much like decisions concerning resource endowment: they are preliminary to the functioning of market exchange and to the consequent attainment of Pareto efficiency. Similar considerations apply to rules that avoid what neoclassical economists refer to as “market failures”: externalities, monopolies, etc. Furthermore, if a legal-economic nexus guarantees the basic rights of workers, the decommodification of the labor force may be envisaged as a possible outcome. What is relevant, here, is that the establishment of one legal system rather than another depends on power relations but also on ethical judgments, which involve a knowledge that transcends markets. Both precede the relative prices that the legal system will lead to. The implication is that the unwanted consequences of the economy depend on the polity: the dismal conditions of

⁷ Polanyi considers a third fictitious commodity, money. We will get back to the role of money further on.

⁸ This argument is very close to Kapp’s (1963). On the relation between Polanyi and Kapp see Swaney and Evers (1989).

working children, for instance, are determined by the absence of a law that effectively forbids child labor.

Just as in the above discussion concerning the identification of efficient prices and institutions, what rights are appropriate cannot be determined according to prices because prices can exist only when those rights are already decided upon. The legal system cannot be improved according to prices because each set of relative prices provides information only in relation to the rights it is based on. Thus, if the legal system is “wrong”, so are the prices it determines: they will provide “wrong” information to whoever bases her choices on them.

7. Opening up the system

Both of the arguments discussed above – the societal reaction to the rationale of price-centered coordination and the regulation of that specific type of coordination – refer to values that are exogenous relative to prices. They reaffirm that coordination is possible only by resorting to a judgment criterion that transcends prices. They, therefore, allow us to go back to the issues concerning the systemic openness of knowledge.

It is precisely this openness of knowledge that provides us with the answers to the questions raised by the above discussion. A judgment criterion exists because people do not just adapt to prices. They do not only learn in strict relation to their economic welfare but also with regard to more general views about their life and their society. Little matters whether their values are mutually consistent or not: indeed, they often tend not to be consistent. Nor is it important that these values sometimes are despicable: the claimed right to exploit or subordinate others – according to their gender, their race or their caste - may indeed be so. What is important is that they exist.

Thus, while people may still explore new ways to make money or to buy the automobile that best fits their wants, they are also likely to seek economic and societal changes that will reduce environmental disruption, maybe by giving greater prominence to public transport. In so doing, they may even be unconcerned about how this will feed back on their own economic welfare⁹. More generally, the way they make their choices cannot be reduced to some – however bounded – optimization procedure¹⁰. A range of other circumstances, determined by their social and natural environment, may concur to how they behave.

The systemic openness of knowledge reflects the absence of boundaries among different dimensions of reality: distinctions between the economy, culture, technology and politics are conventional devices to simplify our attempts to understand the world (Georgescu-Roegen 1976). Real systemic openness implies that the material reproduction of society interacts with other societal dimensions, especially the reproduction of social relations as they evolve historically. This interdependence of the economy with history provides for a better understanding of economic evolution. More specifically, it not only suggests that markets do not always coincide with price coordination of provisioning. It suggests that, over time, the material reproduction of society may have undergone a significant change relative to its social reproduction. Veblen’s analysis of the shift from 19th Century capitalism to modern capitalism, Keynes’ reference to a monetary production economy and Marx’s emphasis on the shift from a simple reproduction to an extended

⁹ This is just another way to express Sen’s (1982) view that people may be concerned about societal issues – e.g. the death penalty – that have nothing to do with their preferences.

¹⁰ Drawing on Streek (2010), Hellmich (2017: 10) notes that “an extended rational choice decision-function, supplemented by variables for context features, will not correctly describe an individual choice, because individual choices are embedded in an environment of time- and context-depending moral choices that must be recognized to explain a phenomenon.”

reproduction: all of these views suggest that provisioning – the production of goods and services - is not the main goal of modern economic activity but a constraint on the viability of capitalist social relations that are centered on the accumulation of money capital.

From a policy perspective this systemic openness suggests that an alternative way to assess the economy is possible. It may draw on Keynes' view that unemployment and distribution are a scandal, on Veblen's (1904) view that serviceability has little to do with profitability, on Kalecki's (1943) view that power relations prevail over profit, on Braverman's (1974), Marglin's (1976) and Samuel's (1977) claim that technology has less to do with efficiency than with social power relations or Kapp's (1976) view that the present economy is grounded on unpaid social costs. It may question not only what the ends of an economy happen to be but what they should be: whether a better way to organize the economy – not the market as such but the overall social interaction to achieve the material reproduction of society – exists, what type of society it entails, what rights it involves that might prevail over prices.

Summing up, a price-centered allocation mechanism requires some regulation. Such a regulation cannot depend exclusively on the mechanism that it regulates. Its rationale must be defined externally. The knowledge that leads to that rationale is not given once and for all. It may change over time, depending on how learning occurs, i.e. on what problem-solving activities are undertaken, and depending on how these problem-solving activities relate to the historically determined organization of society. Learning may be centered on profit opportunities and relative prices in the case of a Schumpeterian entrepreneur or of a Kirznerian (1973) arbitrageur. It may also be focused on making money, as in the cases outlined by Veblen, Keynes and Marx. At the same time it may have little to do with these strictly economic goals for an individual who – in line with Sen's theoretical contributions - is concerned with a quality of life that transcends prices and commodities, as well as for a member of a community who places values and social commitment before preferences. Truly, from a business perspective, the latter may be considered obstacles. In general, however, they are just different ways to look at the issue.

It is appropriate, here, to shift the discussion from the abstract level maintained so far to a historical, if extremely concise, case study. The following section will therefore deal with something that happened little less than forty years ago but that still has something to teach us.

8. Prices and ... Mitterand

In 1981, the socialist Francois Mitterand decided to enact an expansionary program right after being elected president of France. The policy consisted of a 10% rise in the minimum wage, a shorter working week and an increase in welfare spending. In an international economy where monetarist policies prevailed, the ensuing current account deficit led to two devaluations of the French currency and the subsequent return to a more restrictive policy. The Bank for International Settlements reported that: "In France the 1983 target [for monetary expansion] reflected a tightening of economic policy generally in the context of a large external current-account deficit which had emerged because aggregate demand developments in France were out of step with those abroad." (BIS 1983). The aim of what follows is to discuss neither Mitterand's priorities nor what other measures would have been more appropriate to achieve those priorities. It is to discuss what Mitterand's attempt called into question, independently of possible alternatives.

The linearity of the report obscures a range of policy issues. The fact that "developments in France were out of step" relates to the country's international integration, especially with regard to the freedom of capital movements, which made a capital flight possible when French interest rates dropped. The "large external current-account deficit" relates to the country's international trade integration. The tightening of monetary policy as a means to control aggregate demand

suggests that administrative controls over banks or on the composition of demand – thus of imports – were not deemed possible or appropriate. Similarly, an expansionary policy based on fiscal redistribution rather than on monetary easing was presumably not deemed possible.

It is fairly plausible that, since Mitterand was forced to reconsider his policy, something was wrong with his plan. The question is what was wrong. This is where the discussion in the above sections enters the picture.

One way to consider the Mitterand experiment is that he contrasted market forces, i.e. price-centered coordination of the economy. This view neglects or plays down that the “market forces” were determined by a range of institutions, some of which were mentioned above: at the very least, Mitterand went against prices determined by those specific institutions. Disregard of this issue is mere ideology in the sense of false consciousness.

Another way to look at the issue is to acknowledge that markets are framed by institutions but that whether we talk of “the market” or of institutions makes little difference because those institutions could not change, given international and domestic power relations. These accounts are typical of those economists who must advise governing actors as to the most appropriate actions at a given point in time. Since institutional change generally requires some time, it is reasonable for such “counsellors of the prince” to behave this way. The issue is whether any change should be constrained by the status quo or, alternatively, a step by step process should change the institutions that preclude the desired ends.

A more explicit way to formulate a defense of price-centered coordination is to contend that, although there was nothing eternal about existing institutions, they should not change because they were functional to economic livelihood. It is nonetheless the case that Mitterand’s policy was also concerned with livelihood: that of the least advantaged sections of society. The discussion above suggests that various notions of livelihood are possible, depending on the ethical priorities people have as individuals and as members of communities. The question therefore turns out to be: what livelihood is at issue? One may disagree with Mitterand’s notion of livelihood but that is a matter of value judgment.

Finally, one could argue that Mitterand’s timing was wrong: institutional changes were both necessary and possible but he did not allow for the time to carry out those changes. This seems to be correct but it raises the question: what was supposed to change? The discussion of the Bank for International Settlement’s report refers to a set of international treaties, which were part of the legal system. Other rules probably were not entirely codified. They had to do with the distribution of output and the management of demand and were related to social, political and economic power relations. It is most likely that Mitterand did not realize that his policy goals involved more actions – more institutional change – than he presumably expected. By not acknowledging that his priorities involved – both at the domestic and at the international level - a coordination of the economy that clashed with institutionalized power relations, Mitterand did not only get the timing wrong; he misunderstood the centrality of institutions, thereby failing to overcome what Polanyi (1947) would have termed his obsolete market mentality.

More generally, what is at issue here is not only which specific institutional arrangement is consistent with the pursued livelihood. It is whether there are higher order institutions - such as those pointed out above with reference to Marx, Veblen, Polanyi and Keynes – that are more pervasive and that are inconsistent with the achievement of the pursued livelihood. How these institutions can change lies beyond the scope of this paper. If you do not take them into account, however, you fail to understand how the economy actually operates. A pecuniary economy can hardly be treated as if its goal was to satisfy the needs of consumers with limited resources.

9. The responsibility of wanting the cake and eating it

I began this discussion by contending that it is not possible to hold economists responsible for the situation we are living in because “economists” is too vague a term: there are different strands of thought and economists are not a compact category. I pointed out that classifications based on sociological categories may be useful but they do help to discuss responsibility, which ultimately relates to economic policy. Similarly, specific analytical techniques may be extremely important for the advancement of economic thought but they are generally compatible with extremely varied approaches to economics.

An alternative approach is to distinguish different strands according to the centrality ascribed to prices in the coordination of economic activity. The latter was defined as the activities associated to the material reproduction of society. The conclusion the discussion led to is centered on the systemic openness versus closure of the economy, i.e. whether it is possible to conceive of a coordination that exclusively depends on prices, and on institutions that complement them, rather than on a range of circumstances that involve the overall historically determined societal and natural environment.

Systemic openness implies that the economy can be coordinated by prices, by institutions strictly related to prices and by institutions that are more generally related to the social and societal environment. The economy can be structured and coordinated in different ways, depending on which societal priorities prevail. These may affect the coordination of the economy to the point that the rationale of the latter will change: rather than ensuring the material reproduction of society, subject to its social reproduction, the opposite may be true.

From a methodological point of view the two approaches seek explanations within different fields. The closed system view focuses on the performance of price-centered coordination in relation to internal failures or external shocks. The open systems approach takes a broader range of circumstances into account, including institutions that have nothing to do with prices. Quite independently of how consistent and accurate single inquiries related to the two approaches may be, these general methodological differences – i.e. value judgments concerning what must be investigated – undermine a generally accepted notion of the discipline.

This allows us to consider responsibilities. The generic responsibility whereby a theory or a model proved wrong is not something anyone can be accused of. Similarly, no approach can be refuted on account of its theoretical drawbacks alone. Scholars may well appreciate the shortcomings of their approach and, yet, believe that a possible solution will eventually be found: this is what academic research is all about, after all.

Problems arise, however, because of the absence of a common ground for economic discourse. This may easily lead to open system scholars wanting a cake and eating it as well. More specifically, while the two approaches are methodologically legitimate, they cannot be dealt with as if they were different perspectives within a common framework. As far as scholars within the open systems approach are concerned, they may be responsible for two types of behavior that are both the cause and the consequence of an ideological bias. In order to obtain a reputation as a scientist, they may attempt to play down value judgments and emphasize technicalities. This occurs in two possible ways. The first one is hyper-specialization: scholars become experts in very specific fields to the point that they risk being unable to relate their topic of research to broader policy issues as they were outlined here (Cedrini, Fontana 2017).

The second one is a focus on the shortcomings – in terms of internal inconsistency - of price-centered approaches, with the belief that this will advance economic thought. Doubtless, the critique of the work carried out by others is a normal feature of academic activity. At the same

time, the internal critique of a theory or a model that is based on a “biased” approach can hardly lead to much progress from the perspective of the alternative approach.

Another behavior is related to policy. In order to carry out any discussion about what action is appropriate, it is necessary to seek a common ground. This may easily lead open systems economists to accept what is less disputed - i.e. discussions concerning how policies related to price-centered coordination can affect the economy - rather than question the social and political power relations that define the policy goals. In other terms, assuming that present day policy makers are not particularly forward looking, the risk for an open systems economist is to be a mere consultant – a “Counsellor of the Prince” – rather than act as “Counsellor for a better society”; it is that, by reasonably acknowledging the existing institutional framework, he implicitly legitimates the *status quo*.

These considerations do not claim that it is pointless to seek common grounds for economic dialogue. They do claim that basic methodological differences should be acknowledged. In policy terms, these differences imply that one approach takes into account goals and policy tools that the other does not: those that are not price-centered. Neglect of this difference leads to behaviors that reflect and reinforce an ideology whereby common grounds are given a priori and value judgments are not made explicit (Ramazzotti 2014).

A final consideration regards the relation between extant policy goals – as they result from historically determined circumstances – and potentially alternative goals. Here, too, we are faced with goals that could be achieved if only the appropriate conditions were in place. The issue is how to establish those conditions. To some extent, this is a task even for a typical price-centered approach, neoliberalism, which acknowledges the need for changes in the legal system to make the price mechanism work appropriately: consider, for instance, welfare to work policies. From an open systems perspective, no disciplinary boundary should prevent an appropriate identification of a strategy. Thus, contrary to what one might be tempted to do when reading a major contribution by Kalecki (1943) – namely that there are “political” constraints you can’t eliminate when you pursue full employment – the insight of his contribution is that such a policy cannot be restricted to macroeconomic measures but requires a broader approach, centered on institutional changes that affect power relations within society. Such an outlook on economic policy involves an outlook on society as a whole: if one is actually to pursue a “possible civilization” one needs to be a participant observer.

10. Concluding remarks

The approach followed here was to focus on the key role that relative prices are supposed to have in the coordination of economic activity. The discussion began by pointing out the problems that arise when we try to theorize a pure price-centered market. It then extended the discussion by examining how institutions may or may not fit into such a theory of the market. It pointed out that the only way to overcome some theoretical drawbacks is to conceive of the economy as an open system. It drew on a specific historical event to point out how different strands of thought could interpret it and how these interpretations affected policy prescriptions.

It is unlikely that many economists are going to claim that we can pursue a perfect competition that will eventually lead us to a desirable Pareto efficient general equilibrium. Most economists, however, are likely to claim that markets are important, even though non-Walrasian features should cast some doubt on their contentions: at the very least, these features should beg the question what markets we are talking about. Odd as it may seem, it is as if very few economists care to be full-fledged neoclassicals and, yet, few can do without some reference to price-centrality. Faced with what seems to be the “strange non-death of price economics”, we must

avoid a sterile discussion of assumptions nobody is willing to defend. At the same time, we need to acknowledge that, when it comes to economic policy, some people are more confident than others that markets work and that they are conducive to some desirable outcome.

The difference between price-centered coordination and coordination centered on historically determined institutions reflects less specific models and assumptions than general views of the world, with their methodological differences. From the perspective of open systems scholars this leads to a strong temptation: caring to behave as if economics was unitary while theorizing that it is not. The risk is that especially open systems economists may fail to identify policies that are actually able to transcend prices and the extant institutional setup.

Bibliographical references

- Arthur W.B. (1999) "Complexity and the Economy", in *Science*, 2: 107-9
- BIS (1983) Annual Report: 76; http://www.bis.org/publ/arpdf/archive/ar1983_en.pdf
- Braverman H. (1974) *Labor and Monopoly Capital*, New York, Monthly Review Press
- Bromley, D.W. (1989) *Economic Interests and Institutions - The conceptual foundations of public policy*, New York: Blackwell
- Buchanan J.M. (1991) *Constitutional Economics*, Oxford, Basil Blackwell
- Cedrini M., Fontana M. (2017) "Just another niche in the wall? How specialization is changing the face of mainstream economics", *Cambridge Journal of Economics*, bex003, <https://doi.org/10.1093/cje/bex003>; published: 10 July 2017
- Coase R.H. (1988) *The Firm, the Market, and the Law*, Chicago, Chicago University Press
- Colander D., Holt R. and Rosser B. (2004) "The Changing Face of Mainstream Economics", in *Review of Political Economy*, 16(4): 485-499 [Citations are from the version in Middlebury College Economics Discussion Paper No. 03-27]
- Colander D., Holt R. and Rosser B. (2007) "Live and dead issues in the methodology of economics", *Journal of Post Keynesian Economics*, 30(2):303-12
- Commons J.R. (1924) *Legal Foundations of Capitalism*, New York, Macmillan
- David P.A. (1997) "Path Dependence and the Quest for Historical Economics: One More Chorus in the Ballad of QWERTY", Discussion Papers in Economic and Social History, University of Oxford, 20
- Davis J.B. (2008) "The turn in recent economics and return of orthodoxy", *Cambridge Journal of Economics*, 32(3): 349-366
- Demsetz H. (1969) "Information and Efficiency: Another Viewpoint", in *Journal of Law and Economics*, March
- Dow, S.C. (1996). *The Methodology of Macroeconomic Thought*, Cheltenham, UK: Edward Elgar
- Dow S.C. (2008) "A Future for Schools of Thought and Pluralism in Heterodox Economics", in J. T. Harvey and R.F. Garnett, Jr. (eds.) *Future Directions for Heterodox Economics*, Ann Arbor, MI: University of Michigan Press, pp. 9-26
- Elsner W. (2001) "Interactive Economic Policy:Toward a Cooperative Policy Approach for a Negotiated Economy", *Journal of Economic Issues*, 1: 61-83
- Elsner W. (2015) "Policy Implications of Economic Complexity and Complexity Economics", MPRA Paper no. 68372
- Elsner W., T. Heinrich, H. Schwardt (2015) *The Microeconomics of Complex Economies. Evolutionary, Institutional, Neoclassical, and Complexity Perspectives*, Amsterdam, Elsevier
- Georgescu-Roegen N. (1976) "Process in Farming Versus Process in Manufacturing: A Problem of Balanced Development", in *Energy and Economic Myths. Institutional and Analytical Economic Essays*, New York, Pergamon Press

- Hayek F.A. (1945) "The Use of Knowledge in Society", in *American Economic Review*, also in *Individualism and Economic Order*, London, Routledge & Kegan, 1949: 77-91
- Hayek F.A. (1949) "The Meaning of Competition", in *Individualism and Economic Order*, London, Routledge & Kegan: 92-106
- Hayek F.A. (1978) "The Errors of Constructivism", in *New Studies in Philosophy, Politics, Economics and the History of Ideas*, London, Routledge & Kegan
- Hellmich S.N. (2017) "What is Socioeconomics? An Overview of Theories, Methods, and Themes in the Field", in *Forum for Social Economics*, 1: 3-25
- Kalecki M. (1943) "Political Aspects of Full Employment", in *Political Quarterly*, vol. XIV
- Kapp K.W. (1976) "The Open-System Character of the Economy and its Implications", in K. Dopfer (ed.) *Economics in the Future: Towards a New Paradigm*, London, Macmillan
- Keynes J.M. (1973) "A Monetary Theory of Production", in D. Moggridge (ed) *Collected Writings of John Maynard Keynes*, vol. XIII, London, Macmillan: 408-411
- Kirzner I.M. (1973) *Competition and Entrepreneurship*, Chicago, Chicago University Press
- Marglin S.A. (1976) "What Do Bosses Do? The Origins and Functions of Hierarchy in Capitalist Production" in A. Gorz (ed.) *The Division of Labour: The Labour Process and Class Struggle in Modern Capitalism*, Brighton, Harvester Press: 13-54
- Marx K. (1867/1990) *Capital, Volume I.*, London, Penguin Books.
- North, D.C. (1990) *Institutions, Institutional Change and Economic Performance*, Cambridge, Cambridge University Press
- North, D.C. (2005) *Understanding the Process of Economic Change*, Princeton, Princeton University Press
- Polanyi, K. (1944) *The Great Transformation*, New York: Holt, Rinehart & Winston
- Polanyi K. (1947) "Our Obsolete Market Economy. Civilization Must Find a New Thought Pattern", *Commentary*, 3: 109
- Ramazzotti P. (2012) "Social Costs and Normative Economics" in P. Ramazzotti, P. Frigato e W. Elsner (eds) *Social Costs Today: Institutional Analyses of the Present Crises*, London, Routledge
- Ramazzotti P. (2014) "Shared economic thought and the neglect of social costs. Reflections on why progressive economists often stick to conventional wisdom", in *Journal of Economic Issues*, XLVIII(4): 1113-1132
- Roepke W. (1960) *A Humane Economy. The Social Framework of the Free Market*, Chicago, Henry Regnery Company
- Samuels, W. (1977) "Technology vis-à-vis institutions in the JEL: A suggested interpretation", in *Journal of Economic Issues*, 11, pp. 871-895
- Samuels W.J., A.A. Schmid, (1997) "The Concept of Cost in Economics" in W.J. Samuels, S.G. Medema and A.A. Schmid (eds) *The Economy as a Process of Valuation*, Cheltenham, Edward Elgar: 208-298.
- Schmid, A.A. (1987) *Property, Power, and Public Choice. An Inquiry into Law and Economics*, 2nd edition, New York: Praeger
- Schumpeter J.A. (1934/2011) *The Theory of Economic Development. An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle*, Transaction Publishers
- Sen A.K. (1982) "Rational Fools: A Critique of the Behavioural Foundations of Economic Theory", in *Choice, Welfare and Measurement*, Oxford, Basil Blackwell: 84-106
- Simon H.A. (1976) "From Substantive to Procedural Rationality", in S.J. Latsis (ed.) *Method and Appraisal in Economics*, Cambridge, Cambridge University Press: 129-148
- Sraffa P. (1960) *Production of Commodities by Means of Commodities. Prelude to a Critique of Economic Theory*, London, Cambridge University Press

- Streek W. (2010) "Does 'behavioural economics' offer an alternative to the neoclassical paradigm?", in *Socio-Economic Review*, 8: 387-397
- Vanberg V.J. (2001) *The Constitution of Markets. Essays in Political Economy*, London, Routledge
- Veblen T. (1904) *The Theory of Business Enterprise*, New York, Schribner's
- Williamson O.E. (1993) "Contested Exchange Versus the Governance of Contractual Relations" in *Journal of Economic Perspectives*, Vol. 7(1): 103-108
- Williamson O.E. (1998) "Transaction Cost Economics: How It Works; Where It Is Headed", in *De Economist*, 1: 23-58
- Witt U. (1998) "Imagination and Leadership - The Neglected Dimension of an (Evolutionary) Theory of the Firm", in *Journal of Economic Behavior and Organization*, April: 161-177