

# Chapter 3: The Relationship Between the Economic System and the Social Order

Is society mainly a market place, in which self-serving individuals compete with one another—at work, in politics, and in courtship—enhancing the general welfare in the process? Or do we typically seek to do both what is right and what is pleasurable, and find ourselves frequently in conflict when moral values and happiness are incompatible? Are we, first of all, ‘normative-effective’ beings, whose deliberations and decisions are deeply affected by our values and emotions?

— Amitai Etzioni<sup>1</sup>

In brief, the principle of self-interest is incomplete as a social organising principle. It operates effectively only in tandem with some supporting social principle. This fundamental characteristic of economic liberalism, which was largely taken for granted by Adam Smith and John Stuart Mill in their different ways, has been lost sight of by its modern protagonists...The attempt has been made to erect an increasingly explicit social organisation without a supporting social morality...In this way, the foundations of the market system have been weakened.

— Fred Hirsch<sup>2</sup>

## Introduction

The previous chapter began an examination of two key, but buried assumptions, which have underpinned much recent public policy formulation: the ideas that the economic system is autonomous and that the economic system has priority over the social system. These two assumptions have allowed economics to become the dominant methodology and vocabulary for the evaluation of public policy choices in our society. As a consequence, ‘economic efficiency’—defined in neoclassical terms—has become the dominant value to be served by government policy.

The discussion so far has centred on the question of how social order originates. It has been shown that there is broad consensus that the social order is a moral order that developed with the social evolution of the human race. It was concluded that there was no pre-social human nature, and consequently the study of social life involved the study of regulated conduct, not simply the study of regularities. It is our shared values that act as the mortar that binds our communities together and these are backed by formal and informal means of

coercion and our own sense of guilt. Importantly, it is the control of our greed that constitutes one of the prime victories of culture over our 'animality'. That victory is, however, incomplete and the maintenance of a peaceful society involves constant struggle. I concluded that, in an effective civil society, the pursuit of individual and organisational choice and 'self-interest' were heavily constrained by internalised moral codes and by externally imposed social sanctions. The resulting order was constantly under threat from what used to be called human sinfulness, particularly human greed.

This chapter will give an account of the various contemporary theories that are used to account for that social order before focusing on the relationship of dependence between the economic and social systems, pointing to the neglect of this relationship by economic fundamentalists. In addition, the chapter will provide a brief historical overview of this debate as it arose after the breakdown of the medieval hierarchical world-view, particularly under the influence of the Reformation.

## **Current Theories Explaining the Existence of Social Order**

Chapter 2 provided an evolutionary account of the development of social order supplemented by a discussion of some of the elements that make up that social order. Among many theorists, however, my evolutionary account will not seem satisfactory as an explanation of our social order, however much the theorist agrees that something like that described really took place. What will often be sought is a satisfying 'theoretical' story providing a causal explanation that is necessarily ahistorical, which attempts to tease out what is 'really' going on in society and what are the 'laws' that determine the way things are. This involves making a distinction between occurrences that are not necessarily associated—that is, contingent—and occurrences that occur closely together, and which are taken to involve some causal relationship. Consequently, such an attempt at causal explanation involves a belief in the existence of some underlying influence or structure or law that creates an objective order, which our culture obliges us to observe and which can be abstracted from historical reality with all its contingent elements in a way analogous to theoretical accounts in the physical sciences. As we will see later, the extent to which there are such underlying structures that are accessible to us is problematic given that this level of abstraction cannot be subject to empirical falsification, as in the physical sciences. The value of such theoretical stories as a means of explanation is, therefore, problematic. The danger is that dialectic is simply substituted for 'proof'.

Such theorising is often distinguished from theoretical accounts that provide a justification for what exists or what is thought to be desirable. The latter does not usually involve an examination of the moral judgements we really make and the values that underlie them, but rather an appeal to some single, plausible

fundamental principle in an attempt to legislate what those moral judgements should be. Often these genuine attempts at explanation and judgement are associated with the theorist's desire to legislate particular judgements about fundamental political and social institutions. The progression of such ideas often involves the attempt by particular theorists to differentiate their stories from those of others. As a consequence, these stories appear to exhibit a developmental trajectory similar to those found in the natural sciences and in industrial development. To me, this Enlightenment project—important though it is claimed to be in providing a justification for our social arrangements—is tainted by an unrealistic apriorism, uni-causal explanations and tenuous and tedious distinctions.

No single dominant story has emerged from these efforts to explain the existence of social order and of our political and moral institutions. Phillips tells us that there are, however, four primary theoretical approaches to the problem:

- the private-interest doctrine
- situational analysis
- the consensus doctrine
- the conflict approach.<sup>3</sup>

The private-interest story assumes that individuals are guided entirely by considerations of self-interest—a view held by economic fundamentalists. Spencer, the most prominent of the *laissez-faire* advocates, is usually cited as a holder of an extreme version of this approach, believing that the pursuit of self-interest formed a self-regulating mechanism in society. Hobbes and Weber are also self-interest theorists who emphasise the inevitability of conflict. In contrast with Hobbes, for Weber, competitive struggles often generate social regularities. George Homans, a well-known contemporary exponent of a private-interest approach, works explicitly with an exchange model based on free-market principles. According to Homans, social interaction is social exchange involving such rewards as esteem, admiration and respect and such costs as boredom, embarrassment and expenditure of time. It is the informal rules governing these exchanges that provide for social order. The problem with such private-interest stories is that they are unable to explain how there could be sufficient similarities among individuals and enough continuity through time to have created organised societies. Nor, as is argued shortly, is it possible to explain all obedience to rules and laws by the calculation of benefits derived from them, or from fear of punishment. The existence of shared social norms is ignored. Such theories have no room for moral notions such as right and wrong. Consequently, they omit the moral dimension in human relations and moral discourse is not even possible.

Erving Goffman, a situational analyst, also sees people as narrowly self-interested, acting out their roles as public means to private ends. For Goffman, society is a

pseudo-moral system in which everyone is engaged busily in the exchange of impressions. Situational morality more generally stresses the importance of the properties and structures of situations in influencing social conduct. Goffman, however, lacks an adequate account of what it is to be human and of human beings possessing a sense of personal identity. Also missing is any commitment to moral standards other than those found in social situations. Nor can he account for moral rules opposed to any derived from those social situations.

The majority of sociologists, including Durkheim and Talcott Parsons, are described as consensus theorists. For these theorists, social order is made possible by a consensus about shared values and meanings. For Parsons, 'institutions or institutional patterns' are defined as '[n]ormative patterns, which define what are felt to be, in the given society, proper, legitimate, or expected modes of action or of social relationship...They are patterns supported by common moral sentiments.'<sup>4</sup>

People are motivated to observe these normative standards through socialisation and social control and through the feelings of self-respect, guilt and shame. Phillips argues that such models are unable to account for social conflict, making too much of control mechanisms and too little of human spontaneity and inner conflict. It is also criticised as a tacit commitment to the *status quo*. More importantly, it is argued that such theorists are not committed to morality as such, only to a moral system that yields order. Such theories can say nothing, therefore, about the moral status of a particular society. Consequently, fears about moral relativism are raised to dispute this tradition. Despite these criticisms, there is much in the consensus approach that is useful. In particular, Phillips agrees with Durkheim, Parsons and most other sociologists that individuals are motivated to act in accordance with normative standards. As argued in Chapter 2, the internalisation of these standards helps provide much of the restraining control necessary for social order. Social order is made possible by consensus within a social system about normative standards; and motivation to observe these standards can best be assured by the mechanisms of socialisation and social control. Phillips, however, is concerned that consensus theorists never consider the possibility of justifying rationally these dominant moral standards. I will argue later that this Enlightenment aspiration for a 'rational' justification of our moral values is unattainable.

Conflict theorists such as Louis Coser and Randall Collins place a strong emphasis on power relationships, coercion, competition and the mechanisms of political allocation. They point to constraint and conflict about values and coercion. For Coser, such conflicts are functional in that they help to structure the larger social environment by assigning positions to the various subgroups within the system and by helping to define the power relations between them. For Collins, however, social life is mainly a fight over the control of resources. What ought to concern

us, according to Collins, is how various factors of power, coercion, control of resources and the like produce particular moral values and beliefs in the first place. For Collins, ethics are ultimately arbitrary—simply a device for dominating others. In the process, Collins assumes that moral principles have only instrumental value. His doctrine makes it impossible to treat one another as moral beings. Phillips goes on to give an account of Alvin Goulder's critique of the functionalist concern with social order. Phillips reduces this to a criticism of the functionalist concern for quiet values such as temperance, wisdom, knowledge, goodness, cooperation or trust and faith in the goodness of God. Nowhere does Goulder formulate and defend his own values.

Similarly, Alan Gewirth attempts to provide a rational justification for moral principles and institutions, avoiding some of the weaknesses of earlier theories, including hypothetical people, hypothetical situations and states of nature. His approach involves trying to deduce these principles from the nature of human action and the web of social relations in which we are embedded. He sees the control of actions for worthwhile ends as inherently social and inter-subjective. He conceives of voluntariness and purposiveness as the most general features of all actions encompassing the effectual, traditional, value-rational and means-ends actions considered by Max Weber. He considers that all actions have a normative structure involving evaluative judgements of the goodness of their purposes, that every agent implicitly makes claims to freedom and well-being as being intrinsically good and accepts logically that all agents have the same prudential generic rights. It follows for Gewirth that every agent must acknowledge certain generic obligations and this leads to his supreme moral principle to act in accordance with the generic rights of your recipients as well as yourself, not just restraining from action damaging to others but contributing positively to their well-being. This obligation extends to social rules and institutions. As Phillips tells us, however, the most influential of contemporary sociological theories of action is that advanced by Parsons. Importantly, however, Parsons does not set out to provide a rational justification for any particular set of moral values—believing that to be impossible. He starts from the concept of an actor whose actions are goal oriented, are involved in situations, are regulated normatively and involve motivation. Because any such actor is involved in interactions with other actors, the outcome of any action is contingent on the response of others. Because the possibility of instability in this situation exceeds the possibility of stability, such actions must be integrated by a shared institutionalised normative order. Of course, this is what was argued in Chapter 2. Without such a normative order, we would be left with the war of all on all.

Summarising the above, there seems to be broad agreement that normative values are significant to human society, though there is less agreement on the positive role they play. Some theories, in stressing their capacity for manipulation in favour of the powerful, invoke effectively a dark account of the human condition

and the doctrine of original sin unmediated by any recognition of the positive contribution of such values to human emancipation—a major theme of Jurgen Habermas's theory of justice, to which we will turn in Chapter 7. My sympathy, along with Phillips', lies with the consensus theories represented by the sociological tradition, and particularly the account given by Parsons. There is, however, no need to reject in their entirety the other perspectives outlined. Clearly, there is some truth in the transactions view of human society; it simply fails to provide anything like a complete account. Indeed, from the perspective developed earlier, it leaves out the bits that are most important. Similarly, there is clearly much conflict in social life and no account should ignore that conflict. Power relationships and coercion are ever-present features of social life and this is one of the main reasons why one should fear an unrestrained market system—as we should fear unrestrained government power. The Christian tradition, with its emphasis on original sin, points to the possibility of abuse of power relations and of moral rules themselves. In summary, there is no need to adopt a uni-causal theory. What does concern me, however, is the attempt by some of these theorists to reconstruct rationally our moral values in accordance with their pet theories and, as a result, to legislate how we should all behave. The evolved social world is much too complex for such reductionism. This was the reason why Aristotle warned us that the good had no universal form and consequently was not reducible to any single principle. So it is much more realistic to acknowledge that the emergence of social order and its maintenance involves a complex of influences over a long period of time.

One important theorist not quite fitting the above is the rational-choice theorist Jon Elster.<sup>5</sup> He does not believe that social norms can be reduced to any single principle—a view given empirical support by the historical account of MacIntyre. In particular, Elster insists that social norms cannot be reduced to rationality or to any other form of optimising mechanism. He argues that such a view cannot deal with the problem of free riding and the voluntary provision of public goods. The rational self-interest of individuals can lead them to behave in ways that are collectively disastrous. He even suggests that a form of irrationality—what he calls magical thinking—plays an important role in many decisions to cooperate. Consequently, Elster entertains briefly the idea that civilisation owes its existence to a fortunate coincidence. He goes on to argue that altruism, envy, social norms and self-interest all contribute in complex, interacting ways to order, stability and cooperation, and provide the cement of society: 'Every society and each community will be glued together, for better and for worse, by a particular, idiosyncratic mix of these motives.'<sup>6</sup>

As already noted, the trouble with nearly all such stories is that—remote from the possibility of empirical falsification—they remain, at the end of the day, speculation. While ideas might be refined and inconsistencies in particular arguments eliminated, conflicting ideas cannot finally be resolved. In addition,

we slip so easily and unconsciously between causal explanations and justification. Explanations advanced as causal rapidly take on normative power. Clearly, it is important to have a vision of who we are to provide some grounding for our decisions, but there is a danger that we can become trapped in a fundamentalist implementation of a particular vision—to the exclusion of other perspectives. Karl Marx is instructive in this regard:

Hitherto men have constantly made up for themselves a false conception about themselves, about what they are and what they ought to be. They have arranged their relationships according to their ideas of God, or normal man, etc. The phantoms of their brains have gained the mastery over them. They, the creators, have bowed down before their creatures. Let us liberate them from the chimeras, the ideas, dogmas, imaginary beings under the yoke of which they are pining away.<sup>7</sup>

Such images are unavoidable if we are to have any discourse at all; and Marx's criticism can be applied with particular potency to his own thinking. The lesson is not to abandon all such visions—an untenable position—but to hold them lightly with some humility, open to other forms of explanation, while acknowledging that the complexity of human society rules out any simple explanatory scheme.

Another approach to explaining the existence of social order seeks an empirical grounding and involves an examination of the development of moral values in growing children. In particular, French developmental psychologist Jean Piaget (1896–1980) conceived of morality as a system of rules for social behaviour, and the essence of morality as the respect that individuals acquired for those rules. Piaget's account of moral development in children up to the age of twelve focuses primarily on its cognitive aspects, though it is not purely a cognitive process. Rather, it is an interactive process during which children's understanding of rules changes. Piaget's account involves a three-stage progression in a child's moral understanding: constraint, followed by cooperation, giving rise to generosity. Piaget sees generosity as a refinement of justice manifest in the concept of equity, which he considers a fusion of justice and love. Piaget noted that altruism, empathy and sharing were all evident in the behaviour of very young children, but he also noted that the legal sense was far less developed in young girls than in boys. In contrast, girls showed a greater capacity for tolerance and innovation in their play. Indeed, Carol Gilligan, a contemporary developmental psychologist, suggests that girls avoid conflict rather than develop rules for limiting its extent, and that Piaget was influenced unduly by his study of boys.<sup>8</sup> There is also good reason to believe that Piaget's account is culturally specific. According to Piaget, five- to six-year-old Swiss children conjecture that nature is just, and he goes on to say that belief in immanent justice wanes with age and experience. Such a development is not, however, true of many in

South-East Asia for whom the natural order is a moral order in which events happen for a moral purpose. Piaget's developmental hypothesis does not hold for Indian children—even if it does hold for Swiss children, something that has also been questioned. Belief in immanent justice does not wane with age among such people.<sup>9</sup>

Lawrence Kohlberg extended Piaget's study of moral development in children into adolescence, modifying Piaget's theory in the process. His is also an interactive theory with three levels of development:

- the pre-conventional, where rules and social expectations are external to the self
- the conventional, where the self has internalised the expectations of others
- the post-conventional, where the self is differentiated from the rules and expectations of others, and values are defined in terms of self-chosen principles. These are further subdivided into two stages. Importantly, he sees the post-conventional level as involving, firstly, a contractual-legalistic orientation and, then, a universal-ethical principle orientation. He suggests that very few people develop to such a stage.

His is a unitary conception of morality as justice, by which he means equality in a democratic society. His account emphasises the role of social institutions in which the basic values of a society are embodied, downplaying the influence of direct teaching. This could be seen as running counter to Freud and the sociological tradition with their emphasis on the internalisation of social values, but there is no necessary opposition between these accounts: they involve a difference of emphasis towards the role of conscious moral reasoning and away from the unconscious—and from tacit moral knowledge. In commenting on Kohlberg's theory, Phillips concludes that cognitive moral development at every stage of moral reasoning is influenced inescapably by unconscious mechanisms, by moral precepts that are acquired earlier and are available consciously and by the moral values and norms of the group and of the wider society.<sup>10</sup> This is demonstrated clearly by the example of Indian children given above.

This difference in emphasis reflects Kohlberg's own commitment to a particular cultural tradition involving a particular type of moral story, which we have already questioned: a rational, unitary account of a morality, based on the concepts of justice and rights in which the rational individual standing alone is the ideal moral agent, entering with rights into fair contracts with others. His interview methodology, however, required his subjects to talk like moral philosophers. This realisation undermines the force of his argument.

Furthermore, rights are only one way of talking about morality. There are other types of moral stories involving fundamentally different starting points in the conception of the self, society and nature, and these do not necessarily take the

form of formal arguments. The latter are very much in the minority.<sup>11</sup> For example, in the Christian tradition, the story of the Good Samaritan carries a particular, powerful moral message, but it is not couched as a formal argument. The similar duty-based theories, however, are another formal way of talking about morality and are concerned with the conformity of individual action to a code of conduct. In the case of India, a duty-based ethical code is combined with a role-based conception of society. Moreover, Kohlberg fails to present any persuasive evidence linking moral reasoning to real behaviour. There is no reason to assume that a capacity to engage in higher levels of moral reasoning leads to moral conduct. If this were so, we would expect there to be a disproportionate percentage of academic moral philosophers among those who engage in heroic good works and who we canonise.

Gilligan argues that Kohlberg's perspective reflects the concern of adolescents justifying by reason their separation from those to whom they were formerly bound. Its limitation lies in its failure to see a world of relationship, compassion and care. Whereas justice emphasises the autonomy of the person, care underlines the primacy of relationship. Kohlberg's theory involves a general neglect of the emotional and behavioural aspects of moral development. In opposition to Kohlberg, Gilligan suggests that moral development proceeds along two different but intersecting paths that run through different modes of experience and give rise to different forms of thought: 'Whereas the analytic logic of justice is consonant with rational social and ethical theories and can be traced through the resolution of hypothetical dilemmas, the ethic of care depends on the contextual understanding of relationship.'<sup>12</sup>

This ethic of care develops through relationships that give rise to an understanding of interdependence and is sustained by the ability to discern connection. The fundamental tension in human psychology between the experience of separation and the experience of connection is reflected in the age-old dialogue between justice and love, reason and compassion, fairness and forgiveness. This tension underlies the conflicting conceptions of the human with which I began this chapter. Gilligan argues that these discrete experiences give rise to two different moral languages: a language of rights that justifies separation, and a language of responsibility that sustains relationships. A focus on the first language at the cost of the second opens the way to manipulation, exploitation and the rationalisation of hurt.

Gilligan's account provides a timely reminder of the dual nature of our Christian inheritance, especially since the Reformation. In Christian language, the life of faith is both corporate and individual. The Christian life is to be lived in community, but it is a life to which individuals as well as communities are called and in which individual conscience is respected. Clearly, there is a tension between these two pillars. The individualistic aspect of Christian

belief—including belief in an individual soul—has been translated into our current secular emphasis on individualism, as an explanatory mechanism and as a normative ideal, through the Enlightenment and its liberal discourse. In Anglo-Saxon countries, however, in contrast with Continental countries, we have lost sight of the communal aspects of the tradition.

Importantly, current work in developmental psychology influenced by Russian developmental psychologist Lev Semenovich Vygotsky (1896–1934) and Russian neuropsychologist Alexander Luria (1902–77) on the social origin of higher mental processes and in particular on the role of spoken language in the shaping of a child’s capacity to think and act, also undermines Kohlberg’s Platonist aspirations.<sup>13</sup> Instead of children’s mental equipment being part of a permanent ‘human nature’ with which all humans alike confront experience, the internalisation of speech is now seen as the means by which children acquire their native culture, their moral values and even their capacity to think. This is consistent with the comparative research on the acquisition of cultural conceptions of the person conducted by social psychologist Joan Miller<sup>14</sup> and, this is consistent with the constructionist view outlined earlier. We have, therefore, come full circle. Our moral values are embedded in the language we are taught as a child and that language is itself a social construct and a social tradition.

I reject Kohlberg’s account, but his emphasis on the role of moral reasoning serves to remind us that social norms are subject to reflection, criticism and revision. Moral philosophers play a role in that reflection, criticism and revision, but their speculations are based also on the ideas and circumstances of their societies. Moral philosophers—economists included—are not the only participants in such moral discourse; it can be seen, heard or read in the media every hour of every day. Nonetheless, moral philosophers help crystallise those ideas.<sup>15</sup>

Despite these long debates—particularly in the sociological discipline—neoclassical economists have neglected to discuss the relationship between the economic system and the broader social system. As contemporary economists Brennan and Buchanan tell us, ‘These economists have tended to neglect the importance of rules under the sometimes naïve presumption that the “market will out”, regardless of institutional constraints.’<sup>16</sup>

In effect, neoclassical economists have endorsed tacitly Margaret Thatcher’s claim that there is no such thing as society and along with it a particularly contentious moral theory. In the process, they are effectively imposing that particular tenuous moral theory on the rest of us, without any moral authority to do so. This conduct reflects the imperialist pretentiousness of neoclassical economics in seeking to explain all social phenomena in defiance of the rest of the social disciplines and the humanities.

Any complex exchange economy needs, and presupposes, an already existing state of general pacification in order to function. Such an economy and its associated institutions are not natural phenomena and they do not arise spontaneously.<sup>17</sup> They are social, historical artefacts. Indeed, the dichotomy between the social system and the economic system is itself a social artefact and is a product largely of the Scottish Enlightenment.

These imperialist tendencies appear even among economists well disposed towards the importance of social norms. For example, contemporary economists Avner Ben-Ner and Louis Putterman<sup>18</sup> label religious prophets as ‘moral entrepreneurs’, presumably on the basis that the language of economic explanation is more ‘scientific’ and more privileged than the traditional religious description. Similarly, these tendencies can be seen in the recent attempts of economists to include our moral concerns within the framework of preferences and consequently within the framework of instrumental and maximising calculation. As argued earlier, however, an economic approach to our moral values—based on the traditional self-interest model—is simplistic and misleading not simply because of the neglect of altruistic behaviour. Among economists, Albert Hirschman (b. 1915) argues against the use of such a simplistic model of human behaviour: ‘What is needed is for economists to incorporate into their analyses, wherever that is pertinent, such basic traits and emotions as the desire for power and for sacrifice, the fear of boredom, pleasure in both commitment and unpredictability, the search for meaning and community, and so on.’<sup>19</sup>

Certainly, minor revisions to the neoclassical model such as allowing bounded rationality or allowing individuals to have altruistic preferences will not be enough to correct this form of modelling.<sup>20</sup> This is because it is simply not true that society consists of a set of independent individuals, each of whom acts to achieve goals that are arrived at independently, and that the functioning of the social system consists of the combination of these independent actions of independent individuals.<sup>21</sup> This billiard-ball view is derived crudely from a number of interrelated influences. Firstly, the only perceptible actors in society are individuals.<sup>22</sup> Secondly, as we will see in subsequent chapters, the political and moral philosophers of the seventeenth and eighteenth centuries—influenced by a mechanical cosmology—built such a view from the Reformation’s emphasis on individual conscience. Thirdly—and largely as a consequence of the first two—individuals are more isolated in modern society than they were in the past. Nevertheless, in modern societies, individuals still do not act independently or set their goals independently; and their interests are still not wholly selfish. The contemporary account of the individual used in much moral and political philosophy and in economics simply does not give us a rich enough account.

The standard response to this critique is the claim that moral values are incorporated into individual preferences; however, this effectively denies the

pervasive, conflicting and regulatory influences of culture. It does so in an attempt to preserve the methodological individualism essential to neoclassical modelling and the primacy of voluntariness essential to its normative use. As I have argued already in Chapter 2, morals are a community construct. It is the assumed conventional dichotomy between the individual and the group that is misleading. It eliminates the tacit, interactive, dynamic relationship between individuals and between those individuals and the cultures within which they are embedded. Treating values as a kind of preference is simply an *ad hoc* strategy to insulate that theory from falsification by eliminating its predictive power and rendering it empty. It also eliminates the distinction embedded in our languages between selfish and unselfish behaviour.<sup>23</sup> The neglect of these considerations is, however, central to the whole neoclassical research program. That program is committed strongly to explanation in terms of methodological individualism, reductionism, instrumental rationality, the Newtonian metaphor and its associated mathematic modelling and self-interest as the fundamental social force. Indeed, the Newtonian metaphor, which is associated with a natural-law outlook, is the dominant metaphor and the master narrative in contemporary economics. These constitute the neoclassical image of what it is to be properly 'scientific'. These commitments are fundamentally normative and misleading rather than positively scientific. Inherent in that commitment is a view of society as a social contract. This is not simply a result of the positivist movement in economics and philosophy for the best part of the twentieth century; it has deeper roots in the whole Enlightenment program, about which more will be said in the next chapter. It provides a particularly good example of how a particular intellectual paradigm or tradition locks us into a particular way of looking and discussing.

While contemporary neoclassical economists have largely neglected the relationship between the economic and social systems, this is not true more generally. It is to the discussion of that relationship by prominent theorists to which we now turn.

The neglect noted above is surprising given the extent of the discussion of the relationship between the social and economic systems since the time of Smith (1723–90). Smith was well aware of the dependency of the economic system on legal rules and institutions; it is a common misrepresentation to regard Smith as the prophet of economic fundamentalism. Sen puts it this way:

While many admirers of Smith do not seem to have gone beyond this bit about the butcher and the brewer, a reading of even this passage would indicate what Smith is doing here is to specify why and how normal transactions in the market are carried out, and why and how division of labour works, which is the subject of the chapter in which the quoted passage occurs. But the fact that Smith noted that mutually advantageous trades are very common does not indicate that he thought

that self-love...could be adequate for a good society. Indeed, he maintained precisely the opposite.<sup>24</sup>

Furthermore, in his best-known work, *The Wealth of Nations*, Smith echoes Hobbes when he says it is 'only under the shelter of the civil magistrate that the owner of that valuable property which is acquired by the labour of many years or perhaps of many successive generations, can sleep a single night in security'.<sup>25</sup>

Earlier, in the *Theory of Moral Sentiments*, he wrote that

in the race for wealth and honours and preferments...[the individual] may run as hard as he can, and strain every nerve and muscle, in order to outstrip his competitors. But if he should jostle or throw down any of them, the indulgence of the spectators is entirely at an end. It is a violation of fair-play, which they cannot admit of.<sup>26</sup>

Importantly, Smith recognised that justice was more a precondition for human interaction, interchange and cooperation than a product of that interaction. What is more, in the *Theory of Moral Sentiments*, Smith argues that economic activity is rooted in the non-economic need for sympathy and appreciation.<sup>27</sup> Economist Lionel Robbins, in talking about Smith's views, suggested that the 'invisible hand' was 'the hand of the law-giver, the hand which withdraws from the sphere of the pursuit of self-interest those possibilities which do not harmonise with the public good'.<sup>28</sup> It is quite clear that for Smith the 'invisible hand' is the hand of God:

[T]he ancient Stoics were of the opinion, that as the world was governed by the all-ruling providence of a wise, powerful, and good God, every single event ought to be regarded as making a necessary part of the plan of the universe, and as tending to promote the general order and happiness of the whole: that the vices and follies of mankind, therefore, made as necessary a part of this plan as their wisdom or their virtue; and by that eternal art which educes good from ill, were made to tend equally to the prosperity and perfection of the great system of nature.<sup>29</sup>

As the above makes clear, Smith was also a Newtonian, seeing the economic system and the social order as a mechanical, equilibrium system involving two fundamental balancing social forces—self-interest and sympathy—and that that balancing was the product of divine providence. Smith, therefore, under the influence of his friend Hume, could be seen as the father of the application of the Newtonian metaphor to economic analysis, just as earlier Hobbes was the father of the application of the Newtonian metaphor to political theory.

This issue of the relationship between society and the economy was central to the work of Karl Marx. He claimed that all distinctively human activity had a social dimension and was made possible only as a result of membership in society.

Cooperation and compassion were more human attitudes than selfish indifference or hostility. He also pointed out that commodities did not go to the market and make exchanges on their own account. Value was not inherent in a commodity; rather, it was a relationship between people expressed as a relationship between things. Consequently, Marx emphasised that the market consisted of social relationships; however, he also told us in his preface to *Contribution to the Critique of Political Economy*:

The totality of these relations constitute[s] the economic structure of society—the real foundation, on which legal and political superstructures arise and to which definite forms of social consciousness correspond. The mode of production of material life determines the general character of the social, political, and spiritual processes of life. It is not the consciousness of men that determines their being, but on the contrary, their social being determines their consciousness.<sup>30</sup>

This is interpreted usually as meaning that the economy constitutes the ‘real foundation’ of society, and on this foundation ‘the legal and political superstructure’ is based.<sup>31</sup> In other words, the moral superstructure of a society is adapted to its socio-technical or economic substructure. This should not, however, be interpreted as meaning that Marx thought that the superstructure was unimportant.<sup>32</sup> Indeed, Berger and Luckmann tell us that the mechanical determinism inherent in the above interpretation misrepresents the dialectical character of Marx’s thought and his real understanding.<sup>33</sup> For Marx, realities were never isolated entities standing in a linear relationship. Rather, reality could be understood only as multifaceted interaction.<sup>34</sup> Nevertheless, he was concerned that human thought was founded in human activity—labour in the widest sense—and in the social relations brought about by this activity. Consequently, Berger and Luckmann suggest that substructure and superstructure should be understood as human activity and the world produced by that activity respectively. Inherent in these views is the belief that there is no such thing as an immutable human nature and that peoples’ wants are largely a function of how society is organised. One consequence is that the various societal forms found in human history are reflected in human self-understanding—a view not inconsistent with the constructionist ideas outlined in Chapter 2. A further consequence for Marx was that the economic elite shaped the perceptions and ideas of the working population, permeating their entire existence: ‘The ideas of the ruling class are, in every age, the ruling ideas: ie, the class which is the dominant material force in society is at the same time its dominant intellectual force.’<sup>35</sup> This is a form of oppression, the source of a false consciousness and of alienation. Of course, these ideas strike at the heart of the idea of individual autonomy and of consumer sovereignty.

In *Capital*, Marx claimed to disclose the 'natural laws' of capitalist production and was perhaps guilty of the same error as the bourgeois economists he criticised: the reification of economic categories and their elevation into universal laws. It was on the basis of these so-called universal laws that he claimed that socialism was a vastly superior form of social organisation to capitalism and that socialism was destined to replace capitalism.<sup>36</sup> Central to these claims was the belief that capitalism debases human beings, reducing them to a state of alienation—an appendage of a machine. Capitalism was a form of society in which the social bond was mutual self-interest, dissolving the social world into atomised individuals confronting each other. It was a system based on the exploitation of the majority—who earned their living by the sale of their labour—by a small minority, who owned the means of production. It was this exploitation that produced class warfare. Nothing less than communism—true democracy—would do away with class antagonisms and enable human beings to live fully human lives. The selfishness and egoism inherent in capitalism were morally reprehensible—the very antithesis of true humanity—and the State and private property were impoverishing human creations, defending the interests of the rich. In particular, the only rights protected in liberal states were those of the egotistical man. Marx believed further that capitalism was incapable of maintaining the full use of the resources of advanced societies, while communism would do so. In addition, communism would produce members of society with better wants and superior accomplishments.

Of course, history has now moved past the Soviet experiment with its problematic connection to Marx's thought and its massive casualty list. Nevertheless, it is no longer possible to maintain a utopian confidence in a socialist alternative to the capitalist system, however much we might decry the failings of the latter. Importantly, that experience has also discredited Marxist thought. In the process, the shared roots in the Enlightenment of Marx's utopianism and that of capitalism are rarely noticed.

The economic sociology tradition dating from Weber regards the economic process as an organic part of society, constantly interacting with other forces.<sup>37</sup> Weber saw economic action as social and emphasised the autonomy of the social orders, law, politics and religion *vis-a-vis* the economy. In opposition to Marx, he argued that it was not the underlying economic forces that created cultural products such as religion and ideology; rather it was culture that produced certain forms of economic behaviour.<sup>38</sup> This emphasis on culture as distinct from economics is said to have been characteristic of Western Marxism and of the Frankfurt school in particular. For example, Habermas argues that people constitute their reality and organise their experience in terms of knowledge-guiding interests, and that Marx's focus on production provides an

inadequate base on which to ground a socially and historically developing rationality.<sup>39</sup>

In *The Protestant Ethic and the Spirit of Capitalism*,<sup>40</sup> Weber argued that the early Puritans, in seeking to glorify God alone and in renouncing the acquisition of material goods as an end in itself, developed certain virtues such as honesty and thrift that were extremely helpful to the accumulation of capital. Weber went on to argue that the reinforcement of social virtues such as honesty, reliability, cooperativeness and a sense of duty to others had the effect of heightening the capacity of adherents to cohere in new communities.<sup>41</sup> This was helpful to economic development because small sectarian communities created natural networks through which businessmen could hire employees, find customers, open lines of credit and the like. Nevertheless, Weber saw market exchange as exceptional in that it represented the most instrumental and calculating type of social action that was possible between human beings. For Dorothy Emmet,<sup>42</sup> the fruitful way of interpreting Weber's views is in terms of the mutual conditioning of one by the other, and this is consistent with the organic outlook of contemporary economic sociology.

For Durkheim, the division of labour serves a much broader function than the creation of wealth and efficiency.<sup>43</sup> For him, it is the principal vehicle for creating cohesion and solidarity in modern society. As the division of labour advances, people cease to bond together on the basis of their similarities (what he called mechanical solidarity) but on the basis of the duties and rights arising out of the interdependency produced by the division of labour (organic solidarity). It is these duties and rights that hold society together. Consequently, morality was central to the whole cohesion of society. Durkheim went on to argue that a whole structure of norms and regulations surrounded economic exchanges and made them possible. In particular, without some generally shared feelings about honest dealings, contracts would be unenforceable.

Durkheim insisted that even a well-functioning exchange economy was in constant danger of being hollowed out by fraud and force. Indeed, Durkheim, in his preface to the second edition of *The Division of Labor in Society*, published in 1902, was concerned about the state of juridical and moral anomie—lawlessness or disconnectedness—which attended economic life in his day:

The most blameworthy acts are so often absolved by success that the boundary between what is permitted and what is prohibited, what is just and what is unjust, has nothing fixed about it, but seems susceptible to almost arbitrary change by individuals. An ethic so unprecise and inconsistent cannot constitute a discipline...

That such anarchy is an unhealthy phenomenon is quite evident, since it runs counter to the aim of society, which is to suppress, or at least to

moderate, war among men, subordinating the law of the strongest to a higher law. To justify this chaotic state, we vainly praise its encouragement of individual liberty. Nothing is falser than this antagonism too often presented between legal authority and individual liberty. Quite on the contrary, liberty (we mean genuine liberty, which it is society's duty to have respected) is itself the product of regulation. I can be free only to the extent that others are forbidden to profit from their physical, economic, or other superiority to the detriment of my liberty. But only social rules can prevent abuses of power. It is now known what complicated regulation is needed to assure individuals the economic independence without which liberty is only nominal.

If in the task that occupies almost all our time we follow no other rule than that of our well-understood interest, how can we learn to depend upon disinterestedness, on self-forgetfulness, on sacrifice? In this way, the absence of all economic discipline cannot fail to extend its effects beyond the economic world, and consequently weaken public morality.<sup>44</sup>

Karl Polanyi takes up much the same theme. For him, the human economy was embedded and enmeshed in institutions—economic and non-economic. The latter were vital.<sup>45</sup> Consequently, Polanyi objected to what he called the economic fallacy of equating the whole of the economy with the market. By doing so, the true nature of the economy was distorted. In *The Great Transformation*,<sup>46</sup> Polanyi disputed Smith's claim that humans had a natural propensity to truck and barter. In *The Economy as an Instituted Process*,<sup>47</sup> he argued that historically there were several different ways of organising an economy: through reciprocity, redistribution and exchange or a combination of all three. Even within markets, prices that fluctuate frequently—due to competition—represent a fairly late stage of development

The market economy as an institutional structure was insignificant until relatively recent times. Nevertheless, the division of labour was a phenomenon as old as society and sprang from differences inherent in the facts of sex, geography and individual endowment. Polanyi believed that historical and anthropological research justified the view that the economy was, as a rule, submerged in social relationships. Economic actors do not act to safeguard their individual interests in the possession of material goods but to safeguard their social standing, claims and assets. Material goods are valued only in so far as they serve this end. In tribal society, an individual's economic interest is rarely paramount as the community keeps its members from starving. It is the maintenance of social ties, on the other hand, that is crucial. Disregarding the accepted code of behaviour would involve cutting oneself off from one's community. In any event, in the long run, all social obligations are reciprocal and serve the individual's long-term interests. In a society characterised by reciprocity, the idea of profit is barred

and haggling is decried, while giving freely is acclaimed as a virtue. As Polanyi said:

Broadly, the proposition holds that all economic systems known to us up to the end of feudalism in Western Europe were organised either on the principles of reciprocity or redistribution, or householding, or some combination of the three. These principles were institutionalised with the help of a social organisation which, *inter alia*, made use of the patterns of symmetry, centrality, and autarchy. In this framework, the orderly production and distribution of goods was secured through a great variety of individual motives disciplined by general principles of behaviour. Among these motives gain was not prominent. Custom and law, magic and religion co-operated in inducing the individual to comply with rules of behaviour which, eventually, ensured his functioning in the economic system.<sup>48</sup>

Consequently, Polanyi believed that what economists saw as the typical market was just one of many possible forms of organised exchange. To Polanyi, two watershed events in European history were responsible for the emergence of the modern market economy: the creation by the mercantilist state of 'internal markets' and the radical elimination of all market regulation beginning in the early nineteenth century in England. To him, the result was unspeakable misery for the common people until actions were finally taken to protect society from 'the self-regulating market'. Consequently, he traces many of the key tragic political events of the twentieth century to the radically utopian attempt in mid-nineteenth century England to transform all of society into one giant market.

For Polanyi, the control of the economic system by the market has overwhelming consequences for the organisation of society: it means no less than the running of society as an adjunct to the market. Instead of the economy being embedded in social relations, social relations are embedded in the social system. A self-regulating market demands nothing less than the institutional separation of society into an economic and a political sphere. To include human beings (labour) and their natural surroundings in the market system is to subordinate the substance of society itself to the market. Consequently for Polanyi, a market economy can exist only in a market society. The very idea of a self-adjusting market implied a stark utopia. He believed that such an institution could not exist for any length of time without annihilating the human and natural substance of society.<sup>49</sup>

The dominant school of economics in the late nineteenth and early twentieth centuries was institutional economics and was associated with such figures as Thorstein Veblen, Wesley Mitchell and John Commons. It was devoted to the investigation of the institutions that underpinned the market economy. It rejected the reductionism of the marginalist school while emphasising the importance of

the legal foundations of an economy and the evolutionary, habituated and volitional processes by which institutions were created and changed.<sup>50</sup> This perspective was not open to mathematical formalism and was eclipsed by neoclassical economics.

Interestingly, Hayek, a strong supporter of market processes and a minimalist state in his later writings, made it clear that what he had called the 'spontaneous' order of the market was dependent on the system of abstract rules, deep-rooted convictions and moral rules, which was the product of civilisation and which represented the institutional infrastructure of the economic system.<sup>51</sup> For Hayek, informal rules such as custom and conventions are probably even more important in daily economic life than the formal ones. Hayek was conscious of the complexity of that social system, arguing that no 'single human intelligence is capable of inventing the most appropriate abstract rules because those rules which have evolved in the process of growth of society embody the experience of many more trials and errors than any individual mind could acquire'.<sup>52</sup>

Another more recent theorist to write on the issue is sociologist Mark Granovetter. He also argues that economic institutions—like all institutions—do not arise automatically in some form made inevitable by external circumstances; they are constructed socially.<sup>53</sup> They are constructed by individuals whose action is facilitated by and constrained by the structure and resources available in the social networks in which they are embedded. Just as for firms and economic groups, how industries are organised is a social construction that often might have been otherwise. He also reminds us that economic action—like all action—is socially situated and cannot be explained by individual motives alone; it is embedded in continuing networks of personal relations rather than carried out by atomised actors. Like Polanyi, he points out that the pursuit of economic goals is accompanied by such non-economic goals as sociability, approval, status and power.

While some economic literature focuses attention on the role of our moral codes in permitting the exchanges involved in any complex division of labour, we would do well to remind ourselves that most economic activity occurs in groups and, without an effective social order, no large-scale group activity would be possible. Indeed, collectives are the important decision-making units in contemporary society. Consequently, Herbert A. Simon (1916–2001) found it puzzling that neoclassical economics placed markets at the centre of the stage with all economic phenomena and all social phenomena to be explained by translating them into, or deriving them from, market transactions based on negotiated contracts.<sup>54</sup> In criticising this approach, Simon pointed to the absence of adequate empirical testing and an absence of an adequate consideration of the literature on organisations and decision making. Because organisations are the dominant feature of the economic landscape, Simon suggests that the term

'organisational economy' might be a more appropriate description than 'market economy'.<sup>55</sup> He also points out that the boundary between markets and organisations varies greatly from one society to another and from one time to another, and argues that these variations need to be explained. Further, he argues that we should begin with empirically valid postulates about what motivates real people in real organisations, and points to four well-documented organisational phenomena: authority, rewards, identification and coordination. Consequently, for Simon, prices are only one of the mechanisms for the coordination of behaviour, either between organisations or within them.

Douglass North (b. 1920) approaches this issue from the perspective of an economic historian interested in explaining economic growth and the differential performances of economies. In *Institutions, Institutional Change and Economic Performance*,<sup>56</sup> he argues that a proper understanding of the nature of human coordination and cooperation has been missing from economic analysis. While many economic historians emphasise the role of technological innovation in the development of human society and in economic growth, North places his emphasis on the development of institutions. He defines those institutions as the humanly devised constraints that shape human interaction and this brings us back into the sociological stream discussed earlier. North sees human cooperation as a fundamental theoretical problem that needs to be explained because complex, impersonal exchange is the antithesis of the condition under which cooperation arises from rational self-interest in game theory. In particular, he sees a vast gap between the relatively clean, precise and simple world of game theory and the complex, imprecise and fumbling way by which human beings have gone about structuring human interaction. He also disputes that evolutionary pressures will lead to institutions that are 'efficient' in the neoclassical sense. He also points out that historically the growth of economies has occurred within the institutional framework of well-developed coercive polities because it is difficult to sustain complex exchange without a third party to enforce agreements.

The difficulty in enforcing agreements has always been the critical obstacle to increasing specialisation and the division of labour. Enforcement poses no problem when it is in the interests of parties to live up to an agreement. Without institutional constraints, however, self-interested behaviour will foreclose complex impersonal exchange because of the uncertainty that either party will find it in their interest to live up to an agreement. Transaction costs will reflect this uncertainty by including a risk premium, the magnitude of which will turn on the likelihood of defection. North argued that throughout history the size of this premium had been too large to allow complex impersonal exchange and therefore limited the possibilities for economic growth.

For North, it has been the evolution of institutions that has limited these costs and in the process created a hospitable environment for the complex exchange necessary for economic growth. Uncertainties surround such complex exchange. They arise as a consequence of the complexity of the problems to be solved and our limited problem-solving abilities. In all societies—from the most primitive to the most advanced—people impose constraints on themselves to give a structure to their relations with others. In these circumstances, history matters because the past, the present and the future are connected to the past by the continuity of a society's institutions. Consequently, today's and tomorrow's choices are shaped by the past.

Such institutions include formal rules and informal constraints such as convention and codes of behaviour. Institutional constraints include what individuals are prohibited from doing and under what conditions some individuals are permitted to undertake certain activities. The rules and informal codes are sometimes violated and punishment is enacted. Therefore, an essential part of the functioning of institutions is the costliness of detecting violations and the severity of punishment. Taken together, the formal and informal rules and the type and effectiveness of enforcement shape the whole character of the social and economic system. Institutions affect the performance of the economy by their effect on the costs of exchange and production. Together with the technology employed, they determine the transaction and transformation costs that make up total costs.

In the course of his analysis, North makes a crucial distinction between institutions and organisations. While organisations—like institutions—provide a structure to human interactions, he differentiates the rules from the players. The institutional framework influences fundamentally what organisations come into existence and how they evolve. In turn, they influence how the institutional framework evolves. Such institutions—from conventions, codes of conduct and norms of behaviour to statute and common law and contracts between individuals—are evolving and are continually altering the choices available to us. Such evolution is a complicated process usually involving incremental change. Even discontinuous changes—such as revolution and conquest—are never completely discontinuous because of the embeddedness of informal constraints in societies. Although formal rules can change overnight as the result of political or judicial decisions, informal constraints embodied in customs, traditions and codes of conduct are much more impervious to deliberate policies. These cultural constraints connect the past with the present and the future and provide a key to explaining the path of historical change.

The institutions necessary to accomplish economic exchange vary in their complexity, from those that solve simple exchange problems to ones that extend across space and time and numerous individuals. The greater the specialisation and the number and variability of valuable attributes associated with a good or

service, the more weight must be put on reliable institutions that allow individuals to engage in complex contracting with a minimum of uncertainty. Exchange in modern economies consisting of many variable attributes extending over long periods of time necessitates institutional reliability, which has emerged only gradually in Western economies. North believes that formal rules make up only a small, although very important, part of the constraints that shape choices in these economies. In our daily interaction with others, whether within the family, in external social relations or in business activities, the governing structure is defined overwhelmingly by codes of conduct, norms of behaviour and conventions. Underlying these informal constraints are formal rules, but these are seldom the obvious and immediate source of choice in daily interactions.

It is clear that exchange is not simple in tribal societies. In the absence of the State and formal rules, a dense social network leads to the development of informal structures with substantial stability. Informal constraints are pervasive features of modern economies as well. These informal constraints involve extensions, elaborations and modifications of formal rules, socially sanctioned norms of behaviour and internally enforced standards of conduct. Cooperative frameworks of economic and political impersonal exchange are at the heart of social, political and economic performance. While formal rules can help, it is the informal constraints embodied in norms and internally imposed codes of conduct that are critical. In short, North<sup>57</sup> does not believe that the rational choice paradigm can explain the historical and contemporary record of economic growth.

In a complementary account, Francis Fukuyama<sup>58</sup> also sees what he calls spontaneous sociability as critical to economic life. His view of the role of moral values in promoting organisational innovation and economic development owes much to the earlier work of Weber and Polanyi. Communities of shared values, whose members are willing to subordinate their private interests for the sake of the larger goals of the community, can alone generate the kind of social trust that is critical to organisational efficiency. Consequently, the ability to create large, private business organisations in such societies as Germany, Japan and the United States is related to the fact that they are high-trust societies with abundant social capital.

Echoing North's<sup>59</sup> and Williamson's<sup>60</sup> focus on transaction costs, Fukuyama argues that widespread distrust imposes a kind of tax on all forms of economic activity—a tax that high-trust societies do not have to pay. Justified expectations of honest conduct in transactions reduce costs incurred finding a buyer or seller, negotiating a contract, complying with government regulations and enforcing that contract in the event of dispute or fraud. There is less need to spell things out in lengthy contracts, less need to hedge against unexpected contingencies, fewer disputes and less need to litigate if disputes arise. In some high-trust relationships, parties do not even have to worry about maximising profits in

the short run, because they know that the other party will make a deficit in one period good later. Importantly, a high-trust society can organise its workplace on a more flexible and group-oriented basis, with more responsibility delegated to lower levels of the organisation. Such a society will be better able to engage in organisational innovation, since the high degree of trust will permit a wide variety of social relationships to emerge. Workers usually find their workplaces more satisfying if they are treated like adults who can be trusted to contribute to their community rather than like small cogs in a large industrial machine designed by someone else. On the other hand, low-trust societies must fence in and isolate their workers with a series of bureaucratic rules. Consequently, the ability of companies to move from large hierarchies to flexible networks of smaller firms will depend on the degree of trust and social capital present in the broader society. This is important in contemporary discussions of the development of electronic commerce and the associated possibility of creating virtual organisations using new communications technology. A low-trust society might never be able to take full advantage of the efficiencies that these developments offer.

Fukuyama argues that the most effective organisations are based on communities of shared ethical values.<sup>61</sup> Such communities do not require extensive contracts and legal regulation of their relations because prior moral consensus gives members of the group a basis for mutual trust. In this regard, Williamson warns us against seeing trust in purely calculative terms, as to do so can have corrosive effects on the relationships involved.<sup>62</sup> Groups can enter into a downward spiral of distrust when trust is repaid with what is perceived as betrayal or exploitation.

Fukuyama, like Stark and Weber, points out that traditional religions—or ethical systems such as Confucianism—constitute the major institutionalised sources of such culturally determined behaviour because their shared moral languages give their members a common moral life. To some extent, any moral community, regardless of the specific ethical rules involved, will create a degree of trust among its members. Certain ethical codes tend to promote a wider radius of trust than others do by emphasising the imperatives of honesty, charity and benevolence towards the community at large.

Fukuyama continues his discussion in terms of social capital, which he defines as a capability that arises from the prevalence of trust in a society or in certain parts of it. Social capital differs from other forms of human capital in so far as it is usually created and transmitted through cultural mechanisms such as religion, tradition or historical habit. The social capital needed to create this kind of moral community cannot be acquired—as in the case of other forms of human capital—through a rational investment decision. Rather, it requires habituation to the moral norms of a community and the acquisition of virtues such as loyalty, honesty and dependability. The group, moreover, has to adopt common norms

as a whole before trust can become generalised among its members. In other words, individuals simply acting on their own cannot acquire social capital. Social capital is based on the prevalence of social rather than individual virtues.

Fukuyama also argues that those societies with a high degree of communal solidarity and shared moral values should be more economically efficient than more individualistic ones. The larger organisations become, the greater the tendency is for individual members to become free riders. The stronger the social solidarity, the more likely it is that members will identify their own well-being with that of the group and the more likely it is that they will put the group's interests ahead of their own. In the words of eminent American Nobel Prize-winning economist Kenneth Arrow:

Now trust has a very important pragmatic value, if nothing else. Trust is an important lubricant of a social system. It is extremely efficient; it saves a lot of trouble to have a fair degree of reliance on other people's word. Unfortunately this is not a commodity that can be bought very easily. If you have to buy it, you already have some doubts about what you've bought. Trust and similar values, loyalty or truth-telling, are examples of what the economist would call 'externalities'. They are goods, they are commodities; they have real, practical, economic value; they increase the efficiency of the system, enable you to produce more goods or more of whatever values you hold in high esteem. But they are not commodities for which trade on the open market is technically possible or even meaningful.<sup>63</sup>

Arrow went on to argue that the whole economic system would break down if it were not for reinforcement agents and incentives based on morality. Elster, however, specifically rejects this as an adequate account of all social norms on the grounds that not all norms are Pareto improvements,<sup>64</sup> some norms that would make everybody better off are missing and the fact that a norm does make everybody better off does not explain why it exists.<sup>65</sup> The last of these would require the demonstration of a feedback mechanism in which the benefits of the norm contribute to its maintenance. In this regard, Elster suggests that a form of social—as opposed to individual—selection could provide an adequate feedback mechanism. Similarly, American sociologist James Coleman<sup>66</sup> (1926–95) concluded that rational-choice theory could not explain the process by which norms were internalised. Furthermore, social psychologist Daniel Batson<sup>67</sup> conducted a series of experiments that went a long way towards disproving that all altruistic behaviour could be explained by the desire to avoid unpleasant feelings or self-punishment or to gain social approval, a sense of efficacy or shared pleasure—a conclusion supported by field research.

In the light of the above, I would argue that our moral, as well as our legal, institutions provide essential infrastructure for the social system in general and

the economic system in particular. Although it has long been recognised that infrastructure is an essential part of the economic system, discussion of that infrastructure is limited mostly to physical infrastructure—a limitation associated with a very poor understanding of the concept of capital. Coleman<sup>68</sup> points to the properties of social capital that distinguish it from the private, divisible, alienable goods treated by neoclassical economic theory. Importantly, while it is a resource that has value in use, it cannot be exchanged easily. Social capital is not the private property of any of the people who benefit from it; it is an attribute of the social structure in which a person is embedded. Social capital does not benefit primarily those whose efforts bring it into existence, but those who are part of the particular structure. The result is that most social capital is created or destroyed as a by-product of other activities. It also means that the importance of social capital is frequently unrecognised.

Of course, the comprehensive legal framework for economic organisation—including property rights and contracts—developed by complex societies also forms an essential part of that apparatus of social control and as such is an essential precondition to any complex division of labour; no one would argue that trust or moral obligation alone could take its place. These institutions are an essential part of any complex market system, but they rest on a bedrock of ethical habits. As Durkheim argues, contracts—which appear to be voluntary, calculated deals among uncommitted individuals—draw effectively on prior shared bonds that are not subject to negotiation, and of which the parties are often unaware.<sup>69</sup>

## Conclusion

Earlier it was argued that two key assumptions had been introduced into contemporary public policy debates by economic fundamentalists. These were the autonomy of the market and the primacy of the market over the social. It has been argued that the complex exchange necessary to a highly specialised division of labour requires a pre-existing state of social peace. That state of peace is dependent on our evolved cultural systems with their informal norms and formal rules backed by formal and informal means of coercion and by our own sense of guilt at the breach of internalised norms. Consequently, the market is a sub-system nestled within a more encompassing societal context. Of course, these systems are not independent of each other: they interact and condition each other. Indeed, social and economic institutions cannot be distinguished clearly.<sup>70</sup> Nevertheless, the process of economic competition is not self-sustaining; its very existence, as well as the scope of transactions organised by it, is dependent to a significant extent on the societal 'capsule' within which that competition takes place.<sup>71</sup>

It has been noted in passing that an evolutionary account of the existence of the social order will not seem to be a satisfactory account to some theorists, who will be looking for an ahistorical account analogous to the theoretical accounts given in the physical sciences. While doubts are entertained about the value of such accounts, and no dominant theory has emerged, a brief overview has been given of the types of theories being advanced in contemporary discourse. It is concluded, however, that there is no need to adopt a uni-causal approach and that all of the accounts discussed provide some insight into the human condition. Of particular importance is the account given by Elster, who concluded that social norms could not be reduced to any single principle and, in particular, could not be reduced to rationality or any other form of optimising mechanism. This brief survey of competing theories ends with an account of the approaches of prominent development psychologists, who have attempted a more empirical approach based on the moral development of children. In particular, Kohlberg's unitary, rationalist conception of morality as justice is discussed and discounted as not providing a convincing account. Gilligan's alternative account of the moral development of children suggests that moral development proceeds along two different but intersecting paths that run through different modes of experience and give rise to different forms of thought: an analytical logic of justice and an ethic of care.

The advocates of social-contract theory, however, work with a model of society that is a replica of the market. Their attempt to model society's moral infrastructure as a social contract is an attempt to reduce all social phenomena to what is itself a particular social phenomenon. It is a contract that takes the simplest of transactions as its paradigmatic example,<sup>72</sup> but a simple exchange transaction provides only a poor model for complex long-term contracts. By trying to generate the rules of economic life internally and by viewing them as having emerged from rational, self-maximising individuals, such theorists have effectively assumed what they set out to explain.

Such a view argues that our long-term interests require the capacity to discipline our appetites—the suppression of our animality—but this argument does no more than incorporate some of our moral values within the concept of self-interest. While it highlights the frequent presence of considerable tension between our immediate desires and our long-term interests, these long-term interests incorporate only some of our moral values. In any event, this concept of self-interest is not descriptive of the real behaviour of real individuals, amounting to no more than idealisations of individuals and of their self-interest—idealisations that fly in the face of daily experience. In any event, as argued earlier, there is no historical basis for the view that fully formed individuals preceded communities and their shared rules, roles and beliefs. Indeed, contemporary society could not exist without the complex of social and religious norms that sustain it. The development of that society—indeed, the

formation of complex communities generally, along with their associated norms and institutions—has been a long process of social evolution along with the development of supporting religious and philosophical beliefs. Of course, it could be said that this process of social evolution produced what amounts to a tacit social contract, but such an assertion would be mere sophistry, devoid of content.

The competition process itself is constrained and sustained by social and legal rules. The complex division of labour in modern societies involves a complex of relationships and institutions, which cannot be reduced to transactions. Rather state, 'law and society are entwined in mutually reinforcing virtuous connection; rather than mutually reinforcing vicious competition. Or so it is when we are in luck.'<sup>73</sup>

The next chapter will focus first on the history of the concept of the social contract and the associated doctrine of freedom of contract as the central paradigms in economic fundamentalism. It will also point to the growing difficulty encountered in trying to justify these theoretical ideas as the original divine basis of natural law was secularised and attempts were made to naturalise it. This leads readily into the question of how economists perceive their own enterprise and how that enterprise fits in with the Enlightenment project.

## ENDNOTES

- <sup>1</sup> Etzioni 1988, p. ix.
- <sup>2</sup> Hirsch 1977.
- <sup>3</sup> Phillips 1986. I have drawn heavily on Phillips for this account.
- <sup>4</sup> Parsons 1949, p. 203.
- <sup>5</sup> Elster 1989.
- <sup>6</sup> Ibid., p. 285.
- <sup>7</sup> Marx and Engels 1970, Preface.
- <sup>8</sup> Gilligan 1982.
- <sup>9</sup> Shweder and Miller 1985.
- <sup>10</sup> Phillips 1986.
- <sup>11</sup> Shweder 1986.
- <sup>12</sup> Gilligan 1983.
- <sup>13</sup> Phillips 1986.
- <sup>14</sup> Miller 1984.
- <sup>15</sup> Downie 1972.
- <sup>16</sup> Brennan and Buchanan 1985, pp. 13–14.
- <sup>17</sup> Polanyi ???
- <sup>18</sup> Ben-Ner and Putterman 1998.
- <sup>19</sup> Hirschman 1983, p. 29.
- <sup>20</sup> Sugden 1998.
- <sup>21</sup> Coleman 1990.
- <sup>22</sup> Ibid.
- <sup>23</sup> Mansbridge 1998.
- <sup>24</sup> Sen 1987, p. 24.

## The Cult of the Market

- <sup>25</sup> Smith 1776, Book V, Ch. 1, cited in Atiyah 1979, p. 327.
- <sup>26</sup> Smith 1757, Part II, Section II, Ch. 11, cited in Atiyah 1979, p. 327.
- <sup>27</sup> Seligman 1992.
- <sup>28</sup> Robbins ????, p. 56, cited in Atiyah 1979, p. 327. We might note in passing that the use of sporting analogies in describing economic competition remains popular to this day. We might also note that it is the controlling set of rules and the mechanism of enforcement that makes such contests possible.
- <sup>29</sup> Meek 1977, p. 10.
- <sup>30</sup> Marx 1961, p. 67.
- <sup>31</sup> Smelser and Swedberg 1994. This brief account of the views of the Economic Sociology School draws primarily on this reference.
- <sup>32</sup> Crotty 1998.
- <sup>33</sup> Berger and Luckmann 1967.
- <sup>34</sup> Crotty 1998.
- <sup>35</sup> Marx 1961, p. 93.
- <sup>36</sup> Conway 1987.
- <sup>37</sup> Smelser and Swedberg 1994.
- <sup>38</sup> Fukuyama 1995.
- <sup>39</sup> Crotty 1998.
- <sup>40</sup> Weber 1930.
- <sup>41</sup> Weber 1978.
- <sup>42</sup> 'In the long run, however, the consequences of the accumulation of wealth by ascetically minded business men made for an erosion of asceticism.' (Emmet 1966, p. 129)
- <sup>43</sup> Durkheim 1993, p. 3.
- <sup>44</sup> *Ibid.*, pp. 2–4.
- <sup>45</sup> Smelser and Swedberg 1994, p. 15.
- <sup>46</sup> Polanyi 1944.
- <sup>47</sup> Polanyi 1957.
- <sup>48</sup> Polanyi 1944, pp. 54–5.
- <sup>49</sup> *Ibid.*, p. 73.
- <sup>50</sup> See [http://en.wikipedia.org/wiki/Institutional\\_economics](http://en.wikipedia.org/wiki/Institutional_economics)
- <sup>51</sup> Frowen 1997.
- <sup>52</sup> Cited in *ibid.*, p. 43.
- <sup>53</sup> Granovetter 1992.
- <sup>54</sup> Simon 1991.
- <sup>55</sup> Simon suggests that the choice of name could matter a great deal, and could strongly affect the choice of variables that are important enough to be included in any first-order theory of the phenomena.
- <sup>56</sup> North 1990.
- <sup>57</sup> North 1998.
- <sup>58</sup> Fukuyama 1995.
- <sup>59</sup> North 1990.
- <sup>60</sup> Williamson 1994.
- <sup>61</sup> Stark defines trust as the expectation that arises within a community of regular, honest and cooperative behaviour—based on commonly shared norms—on the part of other members of that community.
- <sup>62</sup> Williamson 1994.
- <sup>63</sup> Cited in Fukuyama 1995, pp. 151–2.
- <sup>64</sup> See Chapter 8.
- <sup>65</sup> Elster 1989.
- <sup>66</sup> Coleman 1990.
- <sup>67</sup> Cited in Mansbridge 1998.
- <sup>68</sup> Coleman 1990.
- <sup>69</sup> Durkheim 1993.

<sup>70</sup> Ben-Ner and Putterman 1998.

<sup>71</sup> Etzioni 1988.

<sup>72</sup> Atiyah 1979.

<sup>73</sup> Krygier 1996, p. 17.