
REVIEW ARTICLE

The Fallacy of Political Innocence: Some Recent Reviews of Economic Reform

Michael Warby

Hugh V. Emy, Remaking Australia: The state, the market and Australia's future, Allen & Unwin, Sydney, 1993

Stephen King & Peter Lloyd (eds), Economic Rationalism: Dead end or way forward?, Allen & Unwin, Sydney, 1993

Peter Self, Government by the Market? The Politics of Public Choice, Macmillan Australia, Melbourne, 1993

In the immediate postwar period, there was broad intellectual and political agreement that government should grow faster than the economy or the population. The rate of increase was a matter for lively debate, but the direction was challenged only by a few despised dissenters. More recently, scepticism about the ability of government to deliver has greatly increased. The notion that government has become too large and ought to be reduced, though hardly a consensus position, certainly has far more currency than it used to. Government has still tended to grow, but at a reduced rate, and has actually shrunk (at least relative to the economy) in some areas and some years.

The decline of confidence in government has been accompanied by increasing use of market mechanisms. Deregulation and privatisation are worldwide trends. At the same time, economics has expanded in influence and reach. It has become an imperial discipline, reaching into areas covered by political science (public choice theory), criminology (economics of crime) and sociology (economics of sex and marriage). This has produced a range of responses. Some academics have picked up the offered analytical tools and techniques and run with them. Others have reacted with alarm and disdain at both the intellectual and the political trends.

The three books under review are all recent Australian contributions to this debate. *Economic Rationalism: Dead end or way forward?* is based on a conference

Michael Warby is an officer of the Parliamentary Research Service, Canberra.

held at Melbourne University in February 1993. The book suffers the normal problems of conference collections: some lack of focus, and contributions of uneven quality. *Remaking Australia: The state, the market and Australia's future* is an attempt by a political scientist who has taken the trouble to become economically informed to offer an industry-policy direction for Australia. *Government by the Market? The Politics of Public Choice* is an intellectual assault on both the entire public-choice enterprise and the increased use of markets. It critically examines the theoretical basis and the empirical effects of pro-market public-sector reforms in English-speaking countries (UK, USA, Canada, Australia and New Zealand).

Different Intellectual Languages

The two critics of economic reform in King and Lloyd's collection are Michael Pusey, author of *Economic Rationalism in Canberra: A Nation-building State Changes its Mind* (1991) and Robert Manne, editor of *Quadrant* and co-editor of *Shutdown: The Failure of Economic Rationalism and How to Rescue Australia* (1992). Pusey¹ argues that economic rationalism is a narrow and destructive creed that stems from sectional social interests and threatens the social stability of host societies. Manne argues that the economists' claim to special knowledge is false. He has elsewhere characterised economic rationalism as a delusion of ideological zealots that filled the intellectual vacuum created by the collapse of the Keynesian consensus under the stress of stagflation. Pusey wants to rehabilitate state action and to revive the consensus that the state should continue to expand (or at least not shrink in relative size). Manne advocates a return to protection and regulation.

The defenders of economic reform in the collection include Richard Blandy, Geoffrey Brennan, John Freebairn, Allan Fels, and Ian Harper. Yet the reader is struck by the extent to which the critics and the defenders talk past each other. It is not at all clear they are talking the same intellectual language. Both Pusey and Manne exhibit a persistent tendency among the critics: a refusal to offer hostages to fortune by revealing their own assumptions (they cannot be so naive as to believe they do not have any) or providing serious evidence for their own policy prescriptions. They offer plenty of criticism of economics, economists and microeconomic reform, and, with much nostalgia for an idealised policy past, make assertions about the 'real' basis of the success or failure of other economies. But there is little attempt to grapple with the profound changes in the world economy or the complexities underpinning economic success. I am struck far more often by the simplistic and ahistorical nature of the comments of the critics than of the defenders of reform.

Most of the critics have not seriously tried to understand why what Andrew Norton (1993) calls the 'policy alliance' of economic rationalism has come about. To do so would involve having to acknowledge the serious failure of the past policy arrange-

¹ I wrote a response to Pusey's paper that was subsequently published in *Quadrant* (Warby, 1993) and as Chapter 13 in James et al. (1993).

ments they find so congenial. Worse, it would undermine the ultimately simple-minded faith they have in political processes.

Experience matters. The patent failure of the command economies and economic success of the Asian Tigers is a far more potent catalyst for global change than any number of books or articles by economists (though economic theory was hardly absent from policy development in the Tigers; and to have powerful apparent confirmation of theoretical points is very useful). Debt burdens and fiscal pressure on budgets (as expectations from government continually run ahead of willingness to pay for them) have done far more to promote the worldwide trend to privatisation than have the writings of Milton Friedman. The persistence, even apparent increase, in poverty and 'need', despite burgeoning welfare expenditures, clearly acts to undermine willingness to endlessly pay for such expenditures, especially where such flows are identifiably geographical (e.g. from north to south Italy or from west to east Canada). The impact of the information technology coupled with human ingenuity in designing new financial instruments and institutions forced government after government, often reluctantly, into financial deregulation. Any commentator who does not grasp the importance of these *practical* factors simply does not understand what is going on. Pusey and Manne (and also Peter Self) give no impression of having that practical grasp. What I would call the 'fallacy of political innocence' — a selective refusal to look beyond immediate causes to underlying interventions — is evident in all three writers. But the effect of government on commercial and other social processes is so pervasive that to simply presume, as they do, that market outcomes have only market causes is utterly untenable.

The social realm is best conceived as a series of interactive concentric rings. The protective actions of the state provide a safe area for a wide range of social interactions. The health of these interactions then provides the basis for economic activity and representative government. From this flow the other functions of government. Each level interacts with the others. That the protective function is prior does not mean that all, or even most, state functions are to be treated as prior, though Self and Pusey talk as if they are. On the contrary, there is much evidence that democracy is itself derivative: that it works reliably and well only on the basis of a rich network of reciprocal relationships and associations (Putnam, 1994). It is far from clear that expansionary government, or the extended welfare state, is entirely healthy for civil society. An unfortunate feature of the debate about economic rationalism has been its tendency to a reductionist market/state dichotomy. The social realm is much larger than this; at least, it is in decent societies.

For the production, distribution or exchange of resources above subsistence level we have only four mechanisms: market exchange, command, custom and charity. Only the first two are seriously amenable to public policy, but they are very far from exhausting the social realm. Judgments about the balance between market and political mechanisms involve comparing their relative effectiveness in achieving particular ends. Such comparisons can be made intelligently only if we have a reasonable grasp of the *actual* features of both markets and politics. (That political processes may be democratic does not render them any less command mechanisms.) The fundamental

divide between supporters and critics of economic reform lies in their respective attitudes to the characteristics and virtues of political processes. The reformers share a certain scepticism about reliance on political and command processes, while the critics all assume that the practices and norms of power are superior to the practices and norms of commerce.

Naivety and Sophistication

In *Government by the Market?*, Peter Self argues that the empirical evidence does not support public choice analyses of political processes, that collective provision is systematically undervalued by public choice theory, and that 'New Right' critiques have currency because they appeal to selfishness. Much of his commentary implicitly assumes that public provision is public-spirited and effective, though he does acknowledge that competition can lead to better provision than monopoly. A distinct drawback of the book is the tendentious tone, which carries a constant implication of stupidity and/or fecklessness on the part of critics of government and welfarism. Self's use of economic statistics is often highly partial as well. Economic policies often have very mixed effects; Self places great stress on negative outcomes of policies he dislikes without giving very much weight to the other side of the story. He does score several direct hits, however. As a career public servant, I agree with Self that the universalisation of market mechanisms is neither workable nor sensible as a basis for public-sector reform. Problems of accountability and efficiency flowing from the sheer scale and complexity of political action are not solved by the proliferation of pseudo-markets (though these may have a useful transitional role). However, again as a career public servant, I am less convinced than Self is of the disinterestedness of public servants. Particularly in the spending departments, the problem is not so much a cynical selfishness as a tendency to find particular views of the world congenial: views that tend to be both narrow and self-serving. What is done is thought to be self-evidently in the public interest, but attempts to seriously monitor the effects are resisted (a disposition greatly aided by the difficulty of monitoring outcomes rather than processes).

Self's intellectual sophistication does not extend to any serious grasp of changes in the international economy or the modern welfare state's problems of sustainability. His judgments show a deep, naive faith in the rationality of government and political action. His wish to define 'public goods' as simply any good demanded or supplied through political processes (p.38) seems to indicate an antipathy to even theoretical limits on effective state action. For him, democracy is a talisman that wards off evil; his proposals for reform all involve strengthening democratic institutions. But 'democracy' is the bundling together in a rather haphazard way of a vast range of issues for occasional crude mass choice. Politicisation of choices does not necessarily spread or equalise social power. The failures of the command economies, the successes of the Asian Tigers, indeed the sweep of European history, suggest quite strongly that freedom of action is more important than democracy to social progress, however desirable it may be to have both.

Self is a prime example of the observation that intellectual revolutions are not made because people change their minds, but because one generation replaces an-

other. However informed and intelligent his criticisms of public choice can be — and there is certainly much to criticise in what is still a very intellectually underdeveloped area — in a deep sense he just doesn't 'get it', and there is no indication in *Government by the Market?* that he ever will. Some of the inconsistencies in his analysis are explicable in terms of tension between naive faith and intellectual sophistication. He writes at length about the failure to cut the government share of GDP and yet his commentary is full of talk of cutback of services. He raises concerns about the effect of government intrusion on the voluntary sector but displays no grasp of similar problems for households, commerce or social networks generally. He has the familiar problem of the interventionist: how to prevent centralised social functions from being run according to hostile values. Self concedes that there are problems in government provision but he often discusses issues in ways that give no serious weight to such problems. Democracy is clearly a supreme value, but politicians are partisan in ways that make them unreliable — so independent public services are vital. But if they are state-supplied, can they be 'independent'? And if they are independent, how democratic are they?

Self's inconsistencies are easily understood if he is taken to be, as so many critics on the Left are, a standard-bearer for the public-sector middle class. His common presumption of the public-spiritedness of public servants and the supporters of government action, and of the moral fecklessness of people in the private sector and their supporters, is of a piece with this. The conflation of 'government' and 'social' is a standard usage in such writing. Much of his commentary on the market has a very 1960s feel to it: for example, the talk of spreading 'commodification', as if that were not a process which has been going on for millennia and which the welfare state encourages rather than inhibits. Self concedes that the criticisms of actual markets all have their political corollaries, but his substantial commentary gives no real weight to this: the right sort of politics can not only deal with the problems of politics, it can deal with the market's problems as well. His idea of civic engagement is fundamentally a narrowly political one: other social processes do not produce the 'correct' outcomes. Self is aware of the tension between his use of democracy as an overriding value, his often dismissive attitude to actual politicians, and his clear desire for an independent bureaucracy; but this ends up only as another unresolved inconsistency in his outlook. He displays signs of a view of democracy as right intent by empowered permanent officials: the public-sector middle class's creed in a nutshell. He proposes even broader government direction of social processes, including government appointments to the boards of large corporations.

There are really only three fundamental ideas in economics: scarcity or the inevitability of rationing, gains from trade, and the diversity of preferences. All else is elaboration. It is simply not intellectually proper to criticise economists and economic advice without showing at least some willingness to grapple with these fundamental ideas. A truly staggering number of commentators, particularly academics, feel free to comment at length, and often in a highly patronising way, about economics, economists and economic policy and yet appear to have made no real attempt to grapple with the relevant concepts or underlying facts of the matter. At times Self appears to

have undertaken such intellectual engagement. At other times he appears to have understood very little. Sometimes he displays a clear understanding of rationing problems, yet he frequently writes as if shortages of public goods were merely the result of insufficient funding. It does not occur to him that rationing by queue might be the unavoidable alternative to rationing by price.

The Social Market

Hugh Emy, in contrast, grasps the importance of international pressures. In *Femaking Australia* he attempts to distinguish between structural changes in the world economy (which undermine reliance on commodity industries, requiring economic 'modernisation' for which he agrees free-market policies are the appropriate response) and the development of advanced interlinked manufacturing technology and transnational trading networks ('globalisation'), for which he thinks strategic planning and co-operative intervention are required. He does not, however, address the simple reality that the spread of manufacturing technology to low-wage countries committed to market policies is what most threatens the incomes of lower-skilled Western workers.

Emy argues strongly for the continuing need for economic restructuring, for dismantling the institutions and culture of protectionism in order to participate in the higher growth path of high-value manufacture. While still a critic of economic rationalism, which he sees as hostile to his firm belief that state and market should be partners rather than opponents, he nevertheless calls it 'rather more than half right' (p.35). Indeed, he is clearly deeply concerned about the unravelling of popular support for economic reform. He wants restructuring to be done more effectively and to be more concerned with fairness and equality, particularly employment opportunities. Unfortunately, he continually invokes Germany, Sweden and Japan as models: appearing to be far more aware of their past successes than of their current deep structural problems.

Emy raises interesting issues about the importance of industry linkages in modern economies, the difficulties involved in 'sequencing' policy changes and the role of skills. With increasing emphasis on human capital and knowledge as determinants of growth, the plausibility of creating comparative advantages clearly grows. Emy is very much an advocate of the middle way between interventionist protectionism and pure free markets: the 'social market' rather than the protected market or the free market. His problem is that such an approach needs a very good sense of the actual faults and virtues of political processes: something we still lack. (The public-choice theorists will have to work harder. In particular, they will have to take power rather more seriously and embrace a richer psychology.)

Concluding Comments

The critics of economic rationalism all believe in politics as the unfolding of the public interest. Formalising the assumptions of the public-interest model of politics is not hard. They are: there is a public interest; it is discoverable through the political process.

ess; and it can be reliably implemented by officials, either through altruism or because the incentive structure reliably leads to dutiful behaviour.

One looks in vain to Pusey or Emy (or Manne in his other writings) to provide serious demonstration of the circumstances in which such assumptions are warranted, though Emy is clearly far more aware than the others of the need to do so, and Self does discuss the issue. Even Emy talks as if the market's being a 'social construct' and needing moral guidance establishes his case (pp.31-3). But the state is even more of a social construct and even more in need of moral guidance. Neither point in any way establishes either the right or the capacity of the state to fulfil the many aims that Emy, and still more the other critics, wish on it.

Emy aside, all the critics pay lip service to the desirability of markets: they just object to anything more than lip service. For example, Pusey's analysis elsewhere of the two realms that make up 'civil society' — the realms of 'states, bureaucracies and the law' and of 'economies, markets and money' (Pusey, 1993) — looks more generous to markets than it is. His commentary (leaving aside the misrepresentations of economics, the bastardisation of recent history, and the inadequate characterisation of civil society) acknowledges no limits on the realm of government in interfering in the realm of the economy. The latter realm is permitted to exist, but has no authoritative claims beyond that. Even any power it has to set prices (particularly wages) is strictly on a 'grace and favour' basis. Similarly, Self's criticism of the use of the term 'redistribution' on the ground that it presumes some moral basis for the pre-existing distribution, and his belief that government has the right to decree whatever distribution it deems appropriate, show the unlimited nature of his faith in (democratic) government. A greater incitement to the politics of aggrandisement and self-interest is hard to imagine. That there is no serious social legitimacy beyond (or against) democratic politics is clearly the central tenet of Self's personal faith, and also of Pusey's and (perhaps) Manne's.

Much of the debate has focused on attitudes to markets. But this is only half of the matter. It is only by looking at attitudes to politics and political processes that we can fully understand what is dividing market reformers from their intellectual critics.

References

- James, C. et al. (eds) (1993), *A Defence of Economic Rationalism*, Allen & Unwin, Sydney.
- Norton, A. (1993), 'Economic Rationalism: Criticising the Critics', pp.31ff in *Keynote Papers from the Special APSA Session on 'Australia, New Zealand and Economic Rationalism: Parallel or Diverging Tracks?' held on 30 September 1993*, Monash University Institute of Ethics and Public Policy (Occasional Paper No. 7).
- Pusey, M. (1993), 'Economic Rationalism: An Underview', pp.1-14 in *Keynote Papers from the Special APSA Session on 'Australia, New Zealand and Economic Rationalism: Parallel or Diverging Tracks?' held on 30 September 1993*, Monash University Institute of Ethics and Public Policy (Occasional Paper No. 7).

Putnam, R. (1994), 'What Makes Democracy Work?', *IPA Review* 47(1): 31-4.

Warby, M. (1993), 'Scapegoating and Moral Panic', *Quadrant*, July/August: 66-73.