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The Civil Market: Medieval Franciscan Ideas to Solve 21st Century Economic Problems

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CLEMENS LECTURE SERIES 2009

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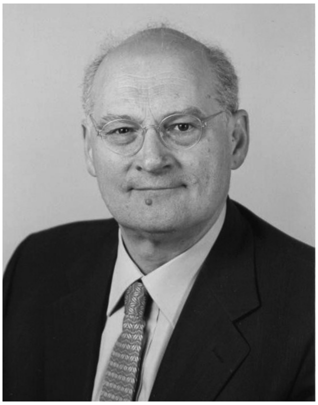

Stefano Zamagni is Professor of Economics at the University of Bologna. He has authored eight books, co-authored seven, and edited more than two dozen others, on various topics, including microeconomic theory, globalization, and most recently such themes as "The Economy of the Common Good" and "Civil Economy."

He is a member of many scholarly editorial boards, and has taught and lectured around the world. He has been a member of the Pontifical Council and Justice and Peace for nearly 20 years, and a member of the Steering Committee of the Pontifical Academy of Social Sciences. In addition to his academic work, he is currently President of Italy's Commission overseeing the work of all charities in the nation.

He was an advisor to Pope Benedict in the drafting of the recent encyclical, *Charity in Truth*. In fact, it doesn't take much detective work in the encyclical to recognize that the Pope has found persuasive much of the work that Professor Zamagni has done on achieving a humane market economy.

He is married to Vera Negri Zamagni and has two daughters and four grandchildren.

Oxford educated, his English is excellent – and his public speaking lively.

The Civil Market:
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Stefano Zamagni

Tonight I want to speak to you about what is called the "civil economy" approach to economics and how it differs from the standard "political economy" approach. The civil economy is a tradition of economic thought which began in the fourteenth and fifteenth centuries, and continued until the middle of the eighteenth century as the dominant one. In the second half of the eighteenth century this way of doing the economic analysis was superseded and replaced by the other one, dominant today, the political economy approach advocated by its founder, Adam Smith.

So the first question I will try to answer is "what is the basic difference between these two ways of doing economic analysis – one called civil economy and the other called political economy?" The second question connected to this is "why is it that in the last 10-15 years we observe, not only in Europe but also here in North America, a resurgence of interest in the civil economy?" Of course, the name "civil economy" is not always used – but that is not important. What is true is that the content of the civil economy approach is gaining more and more attention even in North America. So my second question is "why is that the case?" How do we explain that after almost three centuries when the political economy approach was the dominant one, we observe today a return to an interest in the much older approach?

Now let me start then from the first question. A convenient way to answer is to ask ourselves what are the basic principles of any social economic order. If a society, no matter where or when, wants to progress, not only in the economic sense but also in the moral and social sense, what are the principles on which it is to be based? The first principle is the exchange of equivalent values – this is simply what everybody knows nowadays. In our market economy, anytime I give something to you or I do something for you, you have to give me the equivalent value in exchange. When I go to the bookstore to buy a pen, I have to give the clerk the value of the pen (its price) in order to receive the pen. Now such exchange of equivalents has an ultimate target: to guarantee efficiency. Efficiency is something good. What does efficiency mean? Not wasting resources, because waste is bad. So society is not sustainable unless it is efficient in the allocation of resources.

But there is a second basic principle: redistribution. Redistribution is a principle which says that for a society to be sustainable over time it is not sufficient that society be good at producing wealth. We know from economic history that societies sometimes start declining not because they are inefficient but because they are not good at redistributing the wealth or the income created.

John Maynard Keyes was one those authors who opened our eyes to this fact because a market economy needs people to have purchasing power in order to operate well. The ultimate goal of distribution is to guarantee equity or what people might prefer to call fairness. Equity is an important value, it is an important principle; a society which does not guarantee equity is doomed to failure.

Then there is a third principle: the principle of reciprocity. Now we come to something new. Talking about the exchange of equivalence, efficiency, redistribution, and equity is common. Open any textbook in economics and you will find these words. Different authors might give them different interpretations but on these four words there is a general consensus. When we come to the third principle, the principle of reciprocity, something different occurs, namely, that most people, particularly most economists, do not know what I am talking about.

Why is that so? In a minute I will provide the answer. But let me ask, what is the ultimate purpose of reciprocity principle? The ultimate purpose is fraternity. Fraternity is a word which has been removed from our lexicon. Still, recall the French revolution and how central was the word "fraternity." Liberty, equality, fraternity – these were the three values for which the French fought their revolution. Reciprocity is the principle which allows a society to recognize the link of fraternity among its own members.

What is the difference between reciprocity and the exchange of equivalents? Most people think they're more or less the same. But these two principles are very different. The exchange of equivalents entails a relation between two parties, A and B, whereby person A, say, rents out a house and person B has to pay rent to A. Now what are the characteristics of the exchange of equivalents? First, the determination of the rental price comes before the agreement to exchange. When we have reached an agreement on rent, I give you the keys to my house and you give me the money. The second characteristic is that the relation from B to A is not free – it is contingent on the relation from A to B. Which means, that if I give you the keys to my house you are compelled to pay, and if you do not pay I bring you to court and the judge will, using legal rules, settle it. Once we have entered into a contractual relation freedom does not exist. People are compelled to live up to the terms of the contract.

Now consider reciprocity. In reciprocity, person A might observe that person B is in need of something, whether material needs, spiritual needs, whatever. And out of a sense of gratuitousness A gives something to person B, under the expectation that B will reciprocate to A on a different occasion. In the process of reciprocity, there is no negotiation of price. Second, B is really free not to reciprocate toward A. B is not compelled to reciprocate. There is no crime, no legal standard that might compel people to reciprocate. Still, if B does not reciprocate, A may take action, perhaps ending their friendship or simply thinking less well of B. So you can see the basic difference between these two principles and now your understand why the practice of reciprocity implies fraternity.

In which areas of social life is the principle of reciprocity put into action. The first answer is the family. How would you describe the relationship between parents and children, brothers and sisters? Would you describe them as an exchange of equivalents? Of course not, because if a brother is in need the sister will help him and vice versa. But the same applies to the member of many voluntary associations, such as clubs or other non-profits, where the relationship among the members of an association is not the exchange of equivalents but reciprocity. Of course, I am not saying that that is always the case. There are many families that grew up practicing the exchange of equivalents among themselves and we observe the results. When you introduce in the family the logic of exchange of equivalence, you destroy the family. And there is a lot of evidence coming from psychology as well as from sociology and philosophy proving that.

Having clarified the meaning of the three principles of exchange of equivalents, redistribution, and reciprocity, we can understand the difference between the political economy and the civil economy. Political economy deals only with the first two principles. Civil economy is a way of doing economics whereby all three principles are jointly taken into account. Thus, the civil economy includes political economy but not vice versa. In the second half of the eighteenth century for many reasons, the third principle was left aside, left to be studied by other scholars. Economists would never deny the existence of reciprocity; they would be stupid if they did. They would say, however, reciprocity has nothing to do with economics; it has no place within the market economy. Reciprocity is better to be left to churches, to associations, to families – to be studied in sociology. Economics has no tools to analyze reciprocity or fraternity. That is why before the second half of the eighteenth century the words "reciprocity" and "fraternity," occurred in most books in economics, but after that they disappeared.

So the first conclusion is that the civil economy approach is broad. It includes efficiency, equity, and reciprocity within the market mechanism itself. This is one of the central messages of the encyclical by Pope Benedict XVI, *Caritas in Veritate*. Economics loses its character as a humanistic subject the moment it forgets about reciprocity.

Now, who invented the civil economy way of doing economics? This is a fascinating answer: The Benedictines and the Franciscans beginning in the eleventh or twelfth century. It is really sad to see how we people today do not recognize the strategic role played in our civilization by the Benedictines and the Franciscans.

As you know, in those days there was in the southern part of France the Benedictine Abbey of Cluny. But the monks there started misbehaving a bit, misinterpreting Benedict's rule. They stopped working, even though *Ora Et Labora* (prayer and work) should never be separated. Eventually another group of monks from Cluny broke off and created a new monastery, whose abbot we know as St. Bernard of Clairvaux. These monks criticized their cousins saying "you are chiseling around the Benedictine rules. We have to go back to the original rules." They started working and they generated inventions in agricultural production. The results were that the Abbey became very rich. First of all, because they lived poorly, in the sense that they used only what was necessary. Second, because they received a lot of donations from people who recognized how serious the monks were in interpreting Benedict's rule. Consider the book *Carta Caritatis*. Many things that we know today and practice today were first written in this book, edited by St. Bernard. These historical movements generated a paradox, sometimes called the embarrassment of riches. Why embarrassment? Because the Cistercians who strove for the poverty of Benedict in really practicing the original spirit of Benedict's rule became rich, in a world where nearly all were poor. And St. Bernard, poor fellow, died without being able to solve the paradox.

Now, the problem of the embarrassment of riches was solved by the Franciscans.

The economic insight of the Franciscans was exactly this: If we want work to circulate, we need to invent a new institutional setup. What was the institutional setup? The market economy! In others words the market economy was the invention of the Franciscans, to solve the paradox that the Benedictines were unable to solve. And that is why the Franciscans left the monastery and created the "convents," houses in the midst of the people in the cities. That is the period when this new model of civilization was begun. It is important to keep in mind that the market economy historically was created in order for wealth to circulate. And this idea is much older. Its roots are in the writings of the fathers of the Church, in particular Basil of Caesarea, the bishop of Caesarea in Cappadocia, Asia Minor (what is now Turkey). In the year 370, Basil published a book – on the good use of riches (you should read it; it is only 25 pages long). Basil said riches or wealth is like water in a well. Unless you take the water out from the well, the danger is that the water may go bad. On the other hand, if you draw off some of the water, the spring underneath will regenerate the supply.

This idea of the fathers of the church in the 6th century – that it was the duty of the Christian to generate wealth but at the same time that wealth should circulate – was not new. It was also known to Jews. In the Hebrew language, the word wealth also means blood. Why is that so? Because for the Old Testament wealth is like blood and blood has to circulate inside our body otherwise as we know disaster occurs.

So the Franciscans were able to draw from these Hebraic and Patristic ideas and they invented the market economy. Now the ultimate purpose of this market economy was to generate the common good. Thus the Franciscans created the first banks (in the form of pawn banks), with the first created in Perugia in 1462. After that they spread throughout Europe. A Franciscan invented double entry bookkeeping. Why in the world would a Franciscan do that? Because they needed to teach people – illiterate, uneducated people – to generate wealth and keep it in circulation without hoarding. The joint stock company was invented by the Franciscans in the fifteenth century in Italy, not as many believe , by the British in the seventeenth century. And the ultimate purpose was to generate common good.

When the civil economy approach was superseded by the political economy approach, a transition marked by the publication of Adam Smith's *Wealth of Nations* in 1776, the common good was replaced by total good as the goal of the economy. The ultimate difference between civil economy and political economy is that the civil economy aims at common good, while political economy aims at total good. What is the difference? It is very simple. Total good is sum total of individual good – sum total means g1 + g2 + g3, etc. What is the property of a sum total? The property is that even if some of the numbers are zero, the sum total remains positive. That is the utility logic. According to Jeremy Bentham, the father of the utility analysis, the target of economic policy is to maximize total good. And maximizing total good might entail reducing to zero the good of some person or groups.

Now what is the common good? The common good can be thought of as the *product* of individual goods, which means g1 x g2 x g3, etc. Now how does multiplication work? Everyone understands that if even one factor is nullified the whole product is nullified. Because zero multiplied by one billion is zero. Whereas zero plus one billion equals one billion. So now you understand the meaning of the metaphor I am recommending to you. In the logic of the common good, no one can be sacrificed for the benefit of others.

So in conclusion when the civil economy way of doing economics was superseded by the political economy approach, we observed the switch from the common good to the total good.

Now I have to come to the second question of my presentation. Why is it the case that in the last ten or fifteen years in an unexpected way in different parts of the Western world there is a growing interest again in the civil economy (even though most people do not *call* it the civil economy). I should note that the expression of "civil economy" was not invented by me. It was invented long ago at the University of Naples in Italy, which was the first university in the world to establish a chair in economics, in 1753. Adam Smith did not hold a chair of economics but a chair of moral philosophy. So the first chair was called a chair in civil economy. And the first professor to hold that chair was Antonio Genovesi, an abbot. That is no wonder, because he was following the tradition from the fourteenth century.

Let me go back to the second question. How do we explain that in recent times there is a growing interest in this civil economy way of doing economics? I offer to you three reasons.

The first reason has to do with Angus Maddison, a famous economic historian. He produced a book a few years ago that set out to measure income per capita in the world from 1000 to 2000 A.D. He calculated that in the year 1000, world per capita income was $580. In the year 2000, it was $8000. That is, income per capita was 13 times greater after1000 years. But if we consider the income *distribution* – employing the gini coefficient to analyze how that wealth was distributed among different groups – he found that the inequality between rich and poor in 2000 was about 40 times greater than in 1000. Our world income has increased by 13 times but inequality has increased by 40 times. So the first reason behind the rise in interest in civil economy is that this economy is not sustainable. Why? Because when income inequality in a country passes a certain threshold, the generation of wealth slows.

So it is not only for moral reasons that this process should be studied. It is also economic reasons. You don't need to be an economist to understand why that is the case. If inequality in a country increases, sooner or later that country will start to decline. That is what theory asserts and historical evidence confirms.

So this frustration is why people are now remembering what I call the civil economy approach, because in a civil economy such great inequality is not possible, as it attends to both the creation and distribution of wealth.

In addition, the idea that the economic problem ultimately boils down to maximizing the creation of wealth is very naïve, and it is an obsolete notion of the creation of wealth. Why? The dominant metaphor has been that a rising tide lifts all the boats. This is the outlook that has dominated in the U.S.A. for twenty-five years. Now we know that metaphor is false. Because if you create wealth and you do not pay attention to its distribution, sooner or later the creation itself will cease.

On the other hand many socialists are only interested in the distribution of wealth and do not pay attention to its creation. Similarly, economists often focus only on creating wealth, on the belief that if we expand the economic pie there is more for everybody. Now we know that is not true. That is why the so called neo-liberal view is in deep crisis: Not because it is wrong but because it is incomplete. They consider only the first element of the economic problem – creation of wealth; the true economic problem entails both creation and distribution. So that is the first reason why we observe in recent times a return, so to speak, to the old way of doing economics. Thus we see that the logic of the common good is not against wealth. It is the total good which prevents us from obtaining real progress. The genius of the civil economy is to accept the challenge of creating *and* distributing wealth.

Now there is a second reason for the increased attention to civil economy: the happiness paradox. The happiness paradox was first introduced in the United States by Richard Esterlin, in a paper published in 1974. For the first ten to fifteen years afterwards nearly all the economists in this country and in Europe laughed at him saying, "Richard is a bit mad. Why is he talking about happiness? Why should an economist be worried about happiness? Happiness is philosophical or religious – leave this to those people. We economists are serious people. We should not waste our time." Today, however, this has changed dramatically. Nearly every economist today would agree with Esterlin.

What is the happiness paradox described by Esterlin? When income per capita in a nation is below about $22,000, that was the number in 1974, increasing income per capita will increase happiness. But when average incomes are above $22,000, further increases in income per capita will decrease the happiness index.

Now you may ask how did we obtain the happiness index? The literature nowadays is huge. But basically the happiness index is obtained by aggregating both objective and subjective parameters. Among the objective parameters is the rate of suicide, which is going up every year. For instance in 15 countries of Europe in 2006 there were 64,000 people who died because of suicide. Now have you every seen a happy person who commits suicide? I have never seen it. That is one sign. Other objective parameters are the consumption of psycho-active drugs and the number of divorces. Other, subjective parameters are investigated by directly asking people about their view of their own happiness.

When incomes pass a certain threshold, producing more income decreases happiness. This problem is extremely troublesome for mainstream economics and the political economy. Why? Because it threatens the system, our market economy. In the past the threats to the market economy came from Marxism, from Soviet-style real socialism. That does not exist any longer. Today the real threat to market economy comes from people who are getting fed up and ask, "What is the point of working harder? What is the point of trying to increase productivity if at the end of the day instead of being happier I am less happy?" Answer this question. Why would such a person continue to work hard to get ahead economically?

Today organizing economic life without attending to the spiritual dimension of human beings is doomed to fail. Because happiness has to do with the spiritual, not the materialistic side of life, the political economy approach has been a mistake, since it emphasizes too much the materialistic side. Of course, the material side is important, but it is not the only side.

So the happiness paradox has brought the spiritual dimension to the attention even of mainstream economics. So no wonder there is an interest in going back to the civil economy. And even Nobel Prize winning economist, Gary Becker has said, "I forgot to take into consideration the spiritual dimension." It is rewarding that important people realize this.

There is a third reason for the renewed interest in civil economy. And that has to with the internal organization of firms. The problem is that the traditional capitalistic way of organizing firms has become obsolete, meaning it does not produce productivity growth. Knowledge is of two types: codified knowledge and tacit knowledge. Today, knowledge is essential, but tacit knowledge is more critical than codified knowledge. Codified knowledge was dominant in yesterday's production processes – since those processes were so materialistic. Today tacit knowledge is the dominant form. Tacit knowledge is knowledge that is spread among all those working in the firm, but such knowledge is not readily articulated or shared. So the question is, "how do we mobilize this tacit knowledge?" The answer is that the firm's managers must apply the principle of reciprocity to elicit tacit knowledge, otherwise people will refuse to externalize the tacit knowledge which is in their brains. So in other words, firms must now consider employees as human beings, because until recently the employees were thought of as factors of production not human beings. When you write a production function, output is a function of capital (K) and labor (L) and other elements. Labor in this model is a factor of production, not a group of human beings. Today people are realizing the negative consequences of this. Unless you apply reciprocity, unless you pay attention to employee's personal situations, including family situations, etc. they will not reveal the tacit knowledge needed for creativity and innovation.

It is time to conclude. Now you understand why the civil economy approach is becoming so popular, because it includes what political economy excluded. In my opinion, this is the sign of hope, a hope that our model of civilization will not disappear. If it does disappear, it will be for internal reasons, not due to external forces! It runs the risk of collapse by implosion, not explosion! So that is why to conclude I would like to refer to an old argument by the French philosopher, Blaise Pascal, who said there three orders in life: The order of bodies (esprit de geometrie), the order of heart (esprit de finesse), and the order of charity (which generates the spirit of prophecy).

Today what our society lacks is exactly the third order. Charity! We know the technicalities, sometimes too well. What we are lacking is charity. At the institutional level this is the lack of reciprocity, and it must be included inside the market, not simply outside. It is easy to have reciprocity in other areas of daily life, but the real challenge we have to accept is to introduce inside the market economy the principle of reciprocity, namely, what Pascal called the order of charity.

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