1-1-1989

Self-Interest, Markets, and the Four Problems of Economic Life

Daniel K. Finn
College of Saint Benedict/Saint John's University, DFINN@CSBSJU.EDU

CLEMENS
LECTURE
SERIES

3

1989

Self-Interest, Markets, and the Four Problems of Economic Life

Daniel Rush Finn

CLEMENS LECTURE SERIES

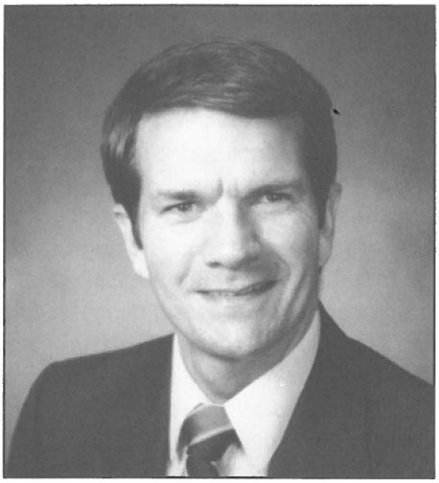
3

1989

Self-Interest, Markets, and the Four Problems of Economic Life

Lecture Delivered By
Daniel Rush Finn, Ph.D

Saint John's University
Collegeville, Minnesota



Daniel Rush Finn

Dr. Daniel Rush Finn was appointed to the William E. and Virginia Clemens Chair in Economics and the Liberal Arts beginning with the 1989-90 school year, succeeding the retiring Dr. Stephen T. Worland, the first occupant of the Chair. Dr. Finn earned the Bachelor of Science degree in mathematics at Saint John Fisher College, Rochester, NY, and did his graduate work at the University of Chicago, completing the M.A. in Economics and the Ph.D. in Religious Social Ethics, with an interdisciplinary dissertation on the ethical presuppositions of utility theory within the history of economic thought. He has held a joint appointment in both economics and theology at Saint John's for the past thirteen years.

Finn has written numerous articles, book reviews and chapters in anthologies on topics relating to economics and ethics within both economics and religious ethics. He is author, along with Prentiss Pemberton, of *Toward a Christian Economic Ethic: Stewardship and Social Power.* He has been an active member of professional societies in both fields, serving as President of the Association for Social Economics and on the Board of Directors of the Society of Christian Ethics. He has also served as President of the Midwest Association of Theological Schools and Vice-President of the Minnesota consortium of Theological Schools. He was Chair of the Department of Economics and Business Administration at Saint John's from 1982-84 and was Dean of the School of Theology from 1984-89.

Overview

During the 1980's we have seen a rise in the public respectability of self interest. One indication of this is the birth of a minor industry designed to help corporations to spend their philanthropic dollars with a clearer view to their own self-interest.[1] As redundant as such an effort may seem to the outsider, many in the United States have felt a newly-robust dignity in asserting self-interest where there may have been at least a tinge of peccability just a decade or two ago.

At the same time, critics of the prevailing market system have re-asserted long-standing objections to economic self-interest. They fault the system for a naive belief that self-interested economic behavior will help the poor by a "trickle-down" effect from the prosperity of the well-off.

This lecture will review a number arguments concerning the proper scope of self-interested economic activity and will provide a framework within which to examine productive efficiency, the distribution of income, and other issues in contemporary debates over the economic system. I will focus on some recent neo-conservative arguments in defense of self-interest in economic life and will fault their overemphasis on the production process. The neo-conservative perspective elevates production, or what is better termed "allocation," to the position of the single most important issue of economic life. However, there are four basic problems of economic life and not just one: the allocation of productive resources to alternative uses, the distribution of income and wealth, the scale of the economy in the biosphere, and the quality of human relations.

To understand how an extreme analytical emphasis on allocation occurred, I will briefly look into the history of the notion of self-interest in economic thought. Major figures like Adam Smith and David Ricardo *did* press for freer markets in the face of prevailing government restrictions on allocation, but their position on appropriate self-interest was more nuanced than their modern-day advocates presume.

After arguing that allocation ought not be viewed as the preeminent economic problem, I will briefly examine all four problems of economic life, and will outline negative and positive interactions. This framework of four problems in economic life cannot of itself solve any one of them; there will continue to be disagreements about the relative importance of the values implicit within and between them. Still, the promise of this framework of four problems is the provision of a clearer view of the various tradeoffs that inevitably exist among the diverse goals at stake in economic policy.

A Note on the Meaning of "Self-Interest"

Allow me to make clear how I intend to use the term "self-interest." In common use, the term often has a pejorative meaning, being associated with "selfish" behavior. The problem with this is that we all recognize occasions where acting to fulfill one's own interests is morally legitimate. When a graduating college senior seeks a job, it is no moral failing to choose the higher paying of two positions which are otherwise equivalent. I am told that nowadays even the monks of St. John's Abbey and the sisters of St. Benedict's Convent are allowed to request their assignments.

Thus, I will use the terms "self-interest" and "self-interested behavior" to refer to "seeking to fulfill your goals", where the intended beneficiary may be the self or may be a complete stranger and where those goals could be morally good or evil or neutral. I will use the phrase "narrowly self-interested behavior" to mean activity where the intended beneficiary is the self, that is, what we normally call "selfish" behavior.

Some Recent Justifications of Self-Interest and Markets

The defense of self-interested action in economic life has a long history, but recent debate on ethics and economics has focused greater attention on the morality of such action and of the economic system known as "democratic capitalism." Critics of the free market's legitimation of narrowly self-interested behavior have long indicted capitalism for its neglect of the poor and unemployed and for its corrosive effects on the moral fiber of individuals and communities. Defenders of the system have stressed the positive effects that capitalism has had, primarily in its economic consequences for the poor and middle class but also in its support of a healthy moral life in the nation.

Perhaps the best known popularizer of this new advocacy of self-interest is George Gilder, who criticizes Adam Smith for relying too much on the workings of self-interest, a phenomenon Gilder downgrades to inconsequence.

> In a capitalist system, the exchange itself is indeed governed by computations of what might be termed self-interest, as the participants negotiate a price agreeable to each. But this self-interest has nothing to do with avarice; it merely reflects a mutual transfer of information, allowing an appropriate allocation of resources.... As Smith showed, this market process, based on morally neutral computations of advantage, is indeed an indispensable instrument for the creation of wealth.[2]

Gilder finds the key in investment, something done by the rich.

> Under capitalism, when it is working, the rich have the anti-Midas touch, transforming timorous liquidity and unused savings into factories and office towers, farms and laboratories, orchestras and museums -- turning gold into goods and jobs and art. That is the function of the rich: fostering opportunities for the classes below them in the continuing drama of the creation of wealth and progress.[3]

Thus it seems that the "morally neutral computations of advantage" by the rich have remarkably positive effects in the production of material prosperity. The primary risk that our nation runs is the well-intentioned but dangerous attempt to improve the system. "The chief threat to this system is taxation with rates so progressive . . . that the rich refuse to risk their money."[4]

Two elements important for our inquiry are at work here. The first is that, according to Gilder, the nation should not attempt to deter self-interested market activity by the rich but should promote it. The second is that morally motivated efforts to improve economic life for the poor or the working class are seen primarily as costly and self-destructively naive withdrawals of resources from the system.

This stress on the role of the businessman and on the primacy of production over distribution is apparent in the work of other theorists as well. Another defender of the capitalist system described entrepreneurs and owners of small businesses in these terms: "[t]these are the people whose hard work creates most of the jobs and ultimately pays the welfare bills."[5]

Even the more carefully drawn defense of democratic capitalism provided by Robert Benne presumes a sort of fundamental priority of production over morality. Art, science, or athletics can lose their reason for being if they become too politicized; Benne argues that the same is true of "economic theory and practice."

> If they are made to bear all the dimensions of human concern, they soon lose any potency of their own or they become so complex as to become completely ineffectual. Indeed, as economizing progresses, enough surplus is created so that those very concerns can be raised, both in economic theory and practice. But though they provide criteria for regulating, guiding, and limiting economic activity, there are no substitute for economizing activity itself.
>
> This hard fact of life -- that moral, social, and political gains are curiously dependent on the relative autonomy of economic efficiency -- is what has been clearly recognized by democratic capitalism.... [6]

> The social wealth produced by economizing does not guarantee a just or good society; but it is a precondition for such a society.[7]

This set of passages does not really constitute a fair characterization of Benne's complete view of the interaction because it does not convey his appreciation of the interplay of communal relationships and productive capacity. Elsewhere in his work he indicates his appreciation of the importance of moral values such as justice and love, but his defense of the market too often reflects the view that the production process is somehow the most basic element and that moral concerns for the quality of human relations are secondary, if not in moral importance at least in the order of empirical possibility. Moral concerns are seen as "costly" and can be "paid for" only out of productive capacity. This is true to some extent, but it is only half the picture. In fact, both basic stone-age production and the modern production process literally *depend* on a moral fabric of existing economic relationships and social institutions, though the fabric was considerably more loosely woven sixty centuries ago.

Michael Novak, perhaps the best-known neo-conservative among American Catholic theologians, sets out to defend a multi-dimensioned democratic capitalism and he, too, argues that critics have long been too hard on the system. In describing the interplay of what he terms economic, political, and moral-cultural systems in democratic capitalism, Novak stresses its humane effects when he argues that

> . . . the problems which the economic system creates for the political and moral-cultural systems are not only well-known but much exaggerated. On the other hand, capitalism has been given far too little credit for what it has done for democracy and what it might, in line with its own ideals, yet do. Similarly with respect to the freedom and vitality of the moral-cultural system.[8]

To be sure, Novak's identification of three separable "systems" that make up the social institution he calls democratic capitalism is an improvement over visions of the economy that do not include any reference to political, social, cultural, religious, and other dimensions of human life that undergird all institutions, including economic ones. Still, his description of the interplay of these three systems leaves the clear impression that the primary problem in our current context is that the political and moral-cultural systems are now or soon will be exercising too much control over the economic system and that we are in the process of killing the goose that lays our golden eggs. This is too simple an analysis of the issues.

While Novak wants to adopt the traditional Smithian view that self-interest is what provides the energy that drives the economy, he nonetheless wants to see it as a "virtuous self-interest."[9] Novak links greed with excessive consumption and associates virtue with investment, identifying the term "self-interest" with

investment only. He contrasts this self-interest with avarice and "short-term advantage." Thus, he says,

> . . . a firm committed to greed unleashes social forces that will sooner or later destroy it. . . .
> Thus, the 'self' in self-interest is complex, at once familial and communitarian as well as individual, other-regarding as well as self-regarding, cooperative as well as independent, and self-judging as well as self-loving.[10]

In Novak's view the character of democratic capitalism makes greed self-defeating. In a sense, this is true for him by definition because he identifies greed with consumption and not investment; however, this should not blind us to the extent to which Novak counts on the tendency of the political and moral-cultural systems to curb the excesses of narrow self-interest that may occur in unscrupulous but profit-maximizing business practices. The political system does this through law and must not, he argues, be called upon too often. The moral-cultural system does this through internal, voluntary boundaries. In this he, like many other, refers to Adam Smith's view as evidence for his own.[11]

Missing in Novak's work, as in many defenses of democratic capitalism, is a clear indication of the criteria according to which moral values held by individuals and communities ought to be legislated through the political process to set limits on economic action. Defenders of capitalism generally accept most of the humanizing "social legislation" enacted over the past one hundred and fifty years, and they now take these adjustments for granted as characteristic of the way any respectable capitalist system should run. If social security, child labor laws, most workplace safety standards, etc., are not up there with apple pie and motherhood, they are close. However, it must be remembered that these political interventions in economic life were originally opposed by most of the wealthy of the day, who argued that each of these government interferences in the market would weaken the economy and ultimately hurt the very persons who were the intended beneficiaries. Of course, these opponents of social legislation were also arguing for their own interests.

Thus, our situation today is as it has been since the beginning of the industrial revolution. Proposals to improve the public morality of the economic process are endorsed or opposed by appeal to both empirical and moral arguments. Empirically the primary issue is whether and to what extent the proposed change will help the intended beneficiaries. Morally, we must inquire whether participants in the public policy debate may legitimately press their own interest in defining policy in the same way they would press their own interests in the market. In addition, we need to ask whether participants in that debate can legitimately employ the justification of market-based self-interest to argue for changes in the laws governing markets to reduce legal restrictions on such self-interested activity there. Putting it concretely, is it morally justifiable for firms or unions (or universities for that matter) to press for their narrow self-interest in Congress or the state legislature?

The moral issue often goes largely unaddressed because the argument that self-interested activity in the market is legitimate is extrapolated to life more generally. The issue is this: If self-interest can be justified "within the game" (here, economic activity in the market), can one thereby justify its extension to debates about the rules of the game (here, in political debate over constraints on the economic system)?

To take an analogy, consider the interplay of self-interest and rules in sports. Within the rules of the game, players and teams are allowed, even expected, to assert their interests in order to win. Assertions that break the rules are penalized. But what should be the attitude of participants engaged in discussions to *set the rules* for the game? Would it be justifiable for, say, athletic directors from colleges in the coldest climates to push for an NCAA rule banning all indoor hockey games and practices? Obviously not, as schools where ambient winter temperatures are above freezing could no longer hope to compete. No longer would the University of Minnesota have to worry about losing to Colorado College.

There can be no simple presumption that because self-interested behavior is justifiable or perhaps even socially beneficial *within* market activities, it is justifiable in determining the rules *governing* market activity. Indeed, the economic self-interest of influential individuals and institutions is today the most powerful force leading to what Michael Walzer has termed the "dominance" of economic goods over goods in other spheres of life.[12] Since there are more problems than simply those the market is adept at solving, greater care is required. Of course, asking this question should not lead us to be so naive as to expect that our answer could prevent the assertion of self-interest in the political realm. Answers to this question about the proper goals and motives of political life are diverse, as the debate between liberal and communitarian perspectives indicates.[13]

A second issue is closely related. Does recognition of the essential role of self-interest within markets serve to justify efforts to reduce existing restraints on self-interested behavior in the market? Does it justify opposition to further proposed restraints intended to achieve goals other than allocation? The answer should be "No." In fact, most business people would cringe if, say, textile manufacturers began to lobby Congress to allow ten-year-olds to hold full-time jobs in the textile mills. Some would argue, of course, that taking ten-year-olds out of school will ultimately reduce national productivity, but most would agree that even if long term productivity were unaffected by the change, it simply wouldn't be right to allow it. Defenders of the system must remember that the only reason that self-interest is justified within markets is that thousands of communal decisions have already been made to restrict many of the abuses which self-interested activity would undoubtedly otherwise cause. The case for self-interest within markets is clearly contingent upon legal and social structures, and thus one cannot validly take the conclusion that narrow self-interest is legitimate in markets and employ that alone as a rationale for altering those very legal and social structures.

Lest ethicists and theologians overblow their own wares, we should also recognize that the traditional aversion to self-interest in Christian ethics is itself a problem. It is often not subtle enough to allow for the moral assertion of self-interest, even by the oppressed. The civil rights movement is an important example of morally justifiable self-interest. The movement for equal rights for women is another.

Still, a closer look at the classic economic defense for self-interest is an important step before examining the four basic problems of economic life and their relevance to the provisional justification of narrow self-interest within markets which democratic capitalism can provide.

Self-Interest and Markets in Adam Smith

The appreciation which Adam Smith had for the motive power of self-interest has been well heralded. We count not on the benevolence of the butcher, the brewer, and the baker when we deal with them but rather on their concern for their own interests.[14] That is, we enter their shops not asking for favors but offering to pay for the goods they purvey. Smith directly advocates the notion of self-interest as a *conceptual tool* for understanding daily commerce, but his advocacy of self-interest as a *human motive* receives only indirect endorsement: it is good to the extent that it is instrumental in promoting human material well-being.

The title of his best known book is telling: *An Inquiry into the Nature and Causes of the Wealth of Nations*. He wrote the book not to raise the level of morality in the nation but to increase its wealth, and he begins by exploring the nature of wealth itself. Smith is quite certainly arguing against what he saw as faulty conceptions of wealth put forth by the Mercantilists and the Physiocrats. Where the Mercantilists often identified wealth with precious metals and the French Physiocrats considered agriculture as the source of all wealth, Smith argued that attention should focus on annual productive capacity, or as he put it, "the annual produce of the land and labor of the society."[15] The emphasis on productive capacity is critical. For Smith, the path to what we would call a higher standard of living for the nation is investment of resources in production.[16] The self-indulgent land-holder who spends his money on consumption is a villain in the economic drama. Smith's view of wealth almost always includes an explicit reference to production *at home*, implying that not just owners but workers also benefited directly.[17] Investment this year in the productive capacity of the nation conduces to greater productivity next year, while lavish consumption reduces the resources left for investment and slowly impoverishes the nation.

Thus, Smith's confidence in self-interest should be seen in its proper context.

He did not conceive self-interest to be a positive force in itself, as it would be from the point of view of ethical egoism. For example, he pointed out the ever-present danger that self-interested business people will be tempted to collude in order to fix prices.[18] Rather, self-interest was positive for him when it contributed to the greater wealth of the nation. Smith had confidence in both self-interest and the market, but the latter was for him more trustworthy. Critical here is his notion of the interaction of self-interested individuals which, for better or worse, has centered on two references he made in all his written work to "the invisible hand."

Many have been the papers published on the notion of Smith's invisible hand, his simile for referring to a purported tendency in life for self-interested behavior to conduce to the common good. Among the more perceptive is one by the political philosopher Joseph Cropsey,[19] who argues that Smith set out to make sense of morality in the face of what he understood to be the modern scientific insight into the determinism of natural causality in nature. Cropsey argues that Smith's efforts should be seen against the backdrop of "a great structure of modern reflection on man's moral condition."[20] Kant answered the necessity of natural causes through the introduction of "an extraordinary higher cause unlike any that operates wholly within the order of nature"; Hume rendered this natural necessity of causes more "mysterious rather than absolute and unshakeable"; and Rousseau looked "to bring the powers of nature to bear upon or against one another" to achieve a norm that lies outside what we currently know as nature.[21] Smith discusses a system of "natural liberty," says Cropsey, "with an innocence that is either thoughtless or farseeing, maintaining as it does a total silence about any possible tension between natural necessity and human freedom." Smith's assumption that nature was both mechanistic and comprehensive, Cropsey concludes, left him with few options other than to adopt "an ancient simplicity: man's integration in the order of nature is beneficial rather than threatening to humanity and is concordant with man's sociality and virtue."

Thus, it was within this framework that Smith was able to assert the identification of self-interest and communal well-being. Take the case of capital investment, in discussion of which appears the single use in the *Wealth of Nations* of the phrase "the invisible hand":

> Every individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of the society, which he has in view. But the study of his own advantage naturally, or rather necessarily leads him to prefer that employment which is most advantageous to the society.[22]

This notion that self-interest contributes to the advantage of society is based on some foundational assumptions for Smith. By making a series of presumptions about economic risks and personal attitudes, Smith concluded that there

is a preference for investing capital at home rather than abroad:

> Upon equal, or nearly equal profits, therefore, every individual naturally inclines to employ his capital . . . to give revenue and employment to the greatest number of people in his own country.[23]

For this reason, the investor's self-interest was described as leading to more employment and production at home by a kind of "invisible hand." Every individual intends only to gain what is of private interest, but the interests of the nation are furthered in the process.

However, where twentieth-century Smithians retain Smith's conclusions about the congruence of individual and communal interests, they remain largely oblivious to his theory of moral sentiments, his interpretation of human freedom in the face of nature's necessity, his definition of national wealth, and even the empirical presumption he made concerning the relative rates of profit at home and abroad. To see the development of this sort of selective reliance, it will be helpful to move on to David Ricardo's theory of comparative advantage and to look back to Smith from there.

The Moral Context Assumed by Ricardo: The Case of Comparative Advantage

Ricardo's theory of comparative advantage was a substantive theoretical contribution to the discipline and as all students of *Introductory Economics* know by this point in the semester, it continues to function as one of the building blocks of today's mainstream economics. It is both fundamental for insiders and frequently counter-intuitive to outsiders. Simply put, the idea of the division of labor asserts that specialization in production will lead toward greater productivity than can be achieved if each person, or town, or nation tries to produce all the items it consumes and therefore engages in no trade. In its most fundamental form, the theory of comparative advantage is an endorsement of Smith's earlier identification of division of labor (i.e., specialization) and interpersonal trade as the keys to increasing wealth.[24] Comparative advantage goes further, however, in asking *which* line of work the individual, town, or nation should specialize in. Let us take Ricardo's now famous example of two nations, the hardest issue.

If England is more efficient than Portugal in producing textiles and Portugal is more efficient than Britain in producing wine, total production in each nation and in both combined is greater when each produces what it is best at and trades with the other country to obtain the other commodity. Portugal should make wine and Britain textiles. More subtly, however, Ricardo's theory of comparative advantage asserts that even if Portugal is more efficient than Britain at producing *both* textiles and wine, if Portugal has a greater advantage in producing wine than in producing textiles (that is, if Portugal has a comparative advantage in producing wine), *both* countries are *still* better off if Britain produces the textiles and Portugal the wine.[25]

In the general interpretation of mainstream economics today, the theory of comparative advantage indicates that "each nation is better off if it engages in free trade with other nations," allowing the self-interested market activity of entrepreneurs and laborers and everyone else to determine the character and growing edges of economic activity. Comparative advantage is generally taken to indicate that *the nation* is better off when *self*-interest is the driving force.

This argument for free trade is pressed in conditions where international capital mobility is far greater than ever before in human history. Many today argue that divestment and plant closings in the United States will nonetheless conduce to the wellbeing of the U.S. as a nation. While no responsible critics of the market would recommend propping up every threatened plant or industry, defenders of the free market position often simply *presume* that financial gains to consumers and to owners of capital outweigh losses to the affected workers.

However, careful study of the texts discloses that the initial insights of the classical economists were far more nuanced and limited than they have often since been taken to be. If, for example, we look carefully at Ricardo's own arguments,[26] we find that in discussing the case where Portugal is more efficient in both lines of production, he observes

> It would undoubtedly be advantageous to the capitalists of England, and to the consumers in both countries, that under such circumstances the wine and the cloth should both be made in Portugal, and therefore that the capital and labor of England employed in making cloth should be removed to Portugal for that purpose.[27]

Yet Ricardo was certainly not about to judge that *the nation* would be better off if all capitalists involved in the textile industry moved their investments to Portugal, with textile workers either moving to Portugal, or more likely, depressing wages in other English industries as they look for work at home. However, he says this problem will not arise for two reasons. First, capitalists tend to prefer not facing the "fancied or real insecurity of capital" in a different country. Second, capitalists share

> the natural disinclination which every man has to quit the country of his birth and connections, and intrust himself, with all his habits fixed, to a strange government and new laws.[28]

As a result, these forces "check the emigration of capital." Thus, in the end, Ricardo simply *presumes* the immobility of capital in his model by arguing that

> these feelings, which I should be sorry to see weakened,

> induce most men of property to be satisfied with a low rate of profits in their own country, rather than seek a more advantageous employment for their wealth in foreign nations.[29]

Risk aversion and national identification just happen to be strong enough to prevent capitalists from rating the likely financial benefits large enough to outweigh the emotional and financial risks. While Ricardo published no theory of moral sentiments like Smith's, his presumptions about the psychological frame of mind of capitalists, and implicitly about the relative advantage of domestic investment over foreign, leave him unconcerned about large scale capital outflows from the nation.

In general, classical political economists did *not* presume that self-interest and markets led in any unconstrained way to the improvement of the nation, *nor* did they presume that the nation's "wealth," taken to mean the nation's economic wellbeing, could increase even if the self-interest of capitalists might lead to foreign investment and higher *aggregate* national wealth at the cost of a widespread drop in the standard of living of the working class. Mainstream economists have adopted the summary statements of the classical and economists about the beneficial interplay of self-interest in markets without accepting their underlying presumptions about the meaning of national wealth or about the cultural constraints upon detrimental forms of international trade.

Generalized Self-Interest in Utility Theory

Classical political economy took a well-documented turn to utilitarianism during the nineteenth century, primarily under the influence of John Stuart Mill. The utilitarian perspective is largely responsible for today's overconfident assessment of the power of markets to solve society's problems. However, that responsibility is an indirect one, and one not neatly attributable to Mill, or even to his intellectual forbears, James Mill and Jeremy Bentham. Utilitarians, of course, had no illusion that self-interested action led directly to the greatest good for the greatest number. Though Mill and the others thought that utilitarian reasoning was applicable to all of society's problems, they regarded economics as far more limited. As he argues in his *System of Logic*, any science, including economics, can be of help in the art of what we would today call public policy, but the limits of science restrict its helpfulness.[30] For Mill, economic science focuses on only one part of human life, that part aimed at increasing wealth. Many other goals compete with this one, and economics cannot adjudicate such differences. From this perspective it would be complete folly to employ insights of economics as a discipline to endorse self-interested behavior other contexts.

Toward the end of Mill's life, however, a simple but mathematically elegant theory for the interaction of individuals' interests in the market was developed. Marginal utility theory constructed a theoretical bridge between the individual's wants and the prices the individual was willing to pay for goods in the market. The structure of the theory was utilitarian, in that all individuals are presumed to act so as to maximize their own utility, though not in the normative sense that every person should act so as to produce the greatest good for the greatest number. By the end of the nineteenth century, marginal productivity theory provided the theoretical bridge between, on the one hand, the utility-maximizing self-interest of owners and workers and, on the other, the willingness of these productive individuals and firms to offer goods or services for sale at various prices in the market. The combination of these two powerful theories into general equilibrium analysis provided, at least in principle, a mathematically determinate explanation for market prices based ultimately on the preferences of individuals. General equilibrium analysis provided a view of economic life based on a psychological starting point which rivaled in perceived comprehension the earlier (and quite different) visions of the French Physiocratic economist François Quesnay and the theory of Karl Marx. It caused a rise in disciplinary self-confidence that is maintained today. By the 1930s, mainstream economists came to understand their discipline as capable of analyzing all human choice under conditions of scarcity.

Given the confidence with which the model of the market and the virtue of self-interest are being invoked in the shaping public policy, it is important to be clear about the presuppositions upon which utility theory rests. A most helpful analysis is that developed in recent decades by the internationally known welfare economist Amartya Sen. Sen argues that the standard economic theory that conceives of individuals as maximizing a utility function depending only on the individual's own consumption has three basic and essentially independent characteristics: a self-centered concept of welfare, a self-welfare definition of goals, and a self-goal restriction of choice.[31]

First, a person's *welfare* is assumed to be *self-centered* in that it is construed to depend only on the person's own consumption. To allow for sympathy, envy, antipathy or other such interpersonal psychic interdependencies would entail losing the mathematical precision that is the core of utility theory's attractiveness as a model. To take an example, consider a college student who is engaged in assessing her activities and interacting with her peers. First, to assume self-centered welfare is to assume that her own welfare is uninfluenced by the problems (or joys) her actions may cause for her roommate (except insofar as this roommate would in turn do something that would directly affect her). She does not get jealous when her roommate takes a luxurious vacation over spring break, and she is not saddened when her roommate grieves the death of a parent. Welfare would fail to be self-centered if the simple knowledge of those events in the lives of others damaged or improved her own welfare.

Second, a person's *goal* is taken in utility theory to be the maximization of his or her *own welfare* (or more precisely, the expected value of his or her own welfare under conditions of uncertainty). That is, whether or not one assumes the person's own welfare to be influenced by the welfare of others, one can still hold that the goal of each person is to maximize his or her *own* welfare, attaching

no importance to the welfare of others. Thus, in the case of the college student in our example, to assume a self-welfare definition of goals would mean assuming that she would not help her friend prepare for a big examination for her friend's sake but only if such activity were perceived to improve her own welfare (either because her friend would reciprocate in some way or, if the notion of self-centered welfare is rejected, because her own welfare is thought to be enhanced by the welfare of her friend).

Third, the *choices* of each person are taken by utility theory to be immediately directed to the attainment of his or her *own goals*, and not those of others. Choices are presumed to be uninfluenced by any recognition of mutual interdependencies of efforts. That is, even though prisoners' dilemma problems indicate that mutual cooperation may lead to aggregate solutions superior to those arising from purely self-interested behavior, utility theory cannot allow for such self-interested suspension of immediately self-interested action. The reason for this is that the individual's environment, including the decisions of other persons, is taken to be "given." Turning to our example, self-goal choice would prevail when the college student acts only to fulfill her own goals (which may or may not be restricted to furthering only her own welfare). This is a complicated issue. As Sen puts it,

> That a person can be expected to choose whichever alternative course of action is best suited to serve his or her goals (including moral objectives if any), given other things on which he or she has no control (including the choices of others), might seem to be entirely reasonable -- perhaps even unexceptionable.[32]

However, knowing how dorm life operates, it is quite likely that this student (and her roommate) will be better off if she and her roommate do *not* immediately pursue only their own goals. Taking into consideration the other's likely response to her actions, our student cannot simply assume, as utility theory does, that the reactions of her roommate are "given." They are, rather, influenced by her actions.

Sen's analysis is helpful and important because it makes clear three distinct meanings of the terms "self-interest" and "self-interested behavior." First, it could mean that one's welfare is uninfluenced by the welfare of others. Second, it could mean that one's goals include only one's own welfare, whether or not one's own welfare is influenced by sympathy, antipathy, etc. Third, it could mean that one's choices are always aimed directly at achieving one's own goals, whether or not those goals include improving the welfare of others.

Because of these discrepant presumptions about human motivation, the current view of self-interest within mainstream economics is confused, difficult to sort out, and apt to shift even within the arguments of a single economist endorsing its advantages.[33] In its most technical sense in utility theory, the concept of self-interest is non-normative and tautological. *All* actions are self-interested in that they arise out of the interests of the self who is acting, whether the intended beneficiary is the self or a friend or a stranger. Of course, in this sense the concept of self-interest is very thin, because by definition, no action could be anything but self-interested. James B. White has argued persuasively that even this limited, "technical" use of the term will encourage self-interest in the normative sense because it structures our conversation and draws attention away from "the reality of community and of shared interests."[34] Remarkably enough, however, this "technical" definition of self-interest as morally neutral has pervasive influence and at times blocks helpful distinctions between morally appropriate and inappropriate forms of self-interest, as when it is employed in the "Lay Letter" published to critique the first draft of the U.S. Catholic bishops' pastoral letter on the economy.[35]

At the same time, when economists claim that in most market interaction people do indeed act out of self-interest they are using the term in normatively weighted sense, calling attention to the fact that the intended beneficiary of the action is the self or a friend or family member. I believe economists are correct in this assertion. But if *this* is the meaning of self-interest, then we are back to the earlier issue of how any justification of self-interest within the marketplace could itself function to justify any change in the rules governing the marketplace. At the very time that economics came to think of itself more generally as directed to analyze *all* human choice among competing goals, its dismissal of earlier Smithian and Ricardian presumptions about human motives left it without the grounds for assuming that self-interested behavior in the market will lead to a greater good.

Depending on the market and self-interested activity within it to "solve" problems can only be justified if it is determined that the market is appropriate to the problem at hand. But the problems facing any modern economy are more diverse than those resolved well within the market, and to an investigation of these problems we now must turn.

The Four Problems of Economic Life

Any attempt to simplify the complexities of life to clarify our understanding entails the imposition of a structure. Thus, the schema of four problems of economic life to be presented here cannot hope to outline the issues in any universally valid manner. It represents a particular perspective on the issues which, I hope, will be helpful in advancing the dialogue between defenders and critics of the current economic system prevailing in most of the Western world. Still it is a perspective and no perspective is trans-perspectival. I suspect that those farther to the right will object because it assigns facticity, or too much facticity, to social entities and underplays the roles and rights of individuals. Others farther to the left will likely find it at least unhelpful, if not actually dangerous, because it grants too much to the neo-conservative argument in

favor of the effectiveness of capitalism.

The critical moral issues approached here clearly transcend economic activity; to approach them from the perspective of the economy alone will mean representing them in a way that is less than full adequate. It is also the case that gathering a multitude of moral issues under a general frame like "the quality of relations" clearly leaves racism, sexism, and many other particular issues unarticulated. This typology also exhibits the deficiencies inherent in focusing on the national economy, rather than international, and on the industrialized countries rather than the Third World. The basic interdependencies among the four problems can be witnessed in every nation and within the international economy as a whole, but I focus on the U.S. in the interest of presenting the argument within time constraints.

I have adopted a broad usage of the term "economic" in identifying "economic problems." From one point of view, it might be preferable to limit the term "economic" more narrowly in an attempt to rein in the over-confidence which some economists have shown in applying economic analysis to all sorts of areas of human life.[36] Nonetheless, "economic issues," broadly construed, already have center stage in public discourse, and it seems more likely that additional concerns might be added to these ongoing discussions under the umbrella of "economic" issues than it does that economic concerns might give way to other, "non-economic" values and goals.

Still, looking at these four basic problems of economic life will, I hope, raise issues in a way that will press all of us to look more carefully at the tradeoffs and interdependencies that exist among and between our most basic goals in our common economic life. Figure 1 gives a rough schema.

Allocation

The first of the four problems to be faced in any economy is that of allocation. The problem itself is an old one in economics, though calling it "allocation" is a twentieth-century phenomenon. The general goal implicit here is the production of goods and services or, in Adam Smith's terms (though not exactly his meaning), the production of wealth. Economists today understand the problem as one of the allocation of resources principally because of a shift in the self-understanding of the discipline. Mainstream economics now understands itself as the study of the allocation of scarce (i.e., costly) resources to alternative uses. The primary value understood to be at stake in this problem of allocation is that of wealth-creation, the production of those goods and services which people find beneficial.

The primary evil confronting efforts at production is waste. Waste can occur in the production process, if more resources than necessary are used to produce a certain amount of a particular good. Waste might also occur at the point of the marketing of products, when the overproduction of a particular good means that

The Four Problems of Economic Life
Figure 1

Problems to be resolved	**General Goal**	**Values**	**Primary Perceived Evils**	**Primary Locus of Decision**	**Major Goal in Current Context**
Allocation	Production	Wealth-creation Efficiency Freedom Self-interest	Waste & inefficiency Government interference Monopoly Monopsony	Market	Increase efficiency
Distribution	Equity	Meeting human needs Security Rewarding productivity effort, risk & sacrifice	Poverty Concentrated wealth Bad incentive structures Self-interest	National community	Reduce inequality
Scale	Sustainability	Conservation/ recycling Limits to growth Appropriate technology	Unsustainable growth Discounting the future	National & world communities	Ecological viability Controlled growth
Quality of Relations	Strong persons in active communities	Individuality/ creativity Community/ participation Culture/ traditions Democracy, freedom, accountability	Loss of individuality Loss of community	Local, regional & national communities	Communal control Responsive bureaucracy

we have more of it than we need or want at current prices and that we should have instead used some of those resources to produce goods in short supply. This understanding of the importance of waste in the process is exactly the point at which the notion of efficiency enters the discussion. No one is in favor of inefficiency. Everyone from profit-maximizing entrepreneurs to environmentally-conscious Christian stewards wants resources to stretch as far as possible.

The primary locus of decision-making in the process of allocation is clearly the market. That is, since individuals and institutions employ resources, it is they who ultimately decide what to do with them, even though these individual decisions are always limited by technological possibilities and relative prices of the era and are often severely constrained by cultural, moral and/or governmental standards. This is true, of course, in more or less capitalist economies, but it is even true to a surprising extent in centrally planned socialist economies. While a socialist government might subsidize the production of rice or bread to make it more easily available, the amount of grain which farmers produce will still be sensitive to the incomes which those farmers receive for producing it.

Because the primary method of governmental influence of persons making market decisions is to offer incentives (for example, tax relief or Pentagon weapons contracts) or impose disincentives (for example, taxes or prison sentences), there is the constant danger that government interference will lead individuals or institutions to react to these new "signals" in ways not foreseen by the legislators who created them. For example, the standard economic argument against rent controls or gasoline price ceilings is that although those people will gain who can find apartments to rent or gasoline to buy, builders of apartments and refiners of gasoline will slow or even cease production of these products, and as a result fewer people will be able to find them for sale. Similarly, without competition in the market, monopoly (one seller), cartels (collusion among sellers), or monopsony (one buyer) will distort proper allocation since persons or organizations with such "market power" will employ that power to their own advantage and to the detriment of others. Anti-trust laws exist to prevent such abuses.

Thus, the problem of allocation features the self-interest of economic actors prominently. Advocates of free markets, of course, also combine this feature with an advocacy of personal freedom as a value in itself, something which in this schema falls under problem four, the quality of relations. This is not an insignificant issue in a world where the people of some nations might lead healthier, better educated lives if more economic decisions were left to the local level. Still, compared to the other three problems, allocation is preeminently dependent on active, free persons and institutions making decisions largely out of their own interests. And the primary goal of those most concerned with the problem of allocation in our current context is to increase efficiency.[37]

Distribution

The second of the four problems is that of distribution, the distribution to individuals and institutions of the products and services available each year. When we ask *to whom* the benefits of the economy should go, we ask a question of equity, and, by and large, economists recognize this. If we were to look at distribution as a problem in isolation from the other three, there come to mind values such as meeting human needs, obtaining security, achieving fair relative incomes, and rewarding productivity, effort, sacrifice, and risk. Much has been written in the history of Christian theology and Western philosophy on the obligations of the well-to-do toward the poor, and this needs to be brought to bear on contemporary discussions. The primary perceived evils in distribution are poverty, the existence of great concentrations of wealth, faulty incentive structures, and the self-interest of persons who "have something to lose" in redistribution. Among institutionalized disincentives are welfare policies that discourage the seeking of employment, legal structures that foster costly litigiousness, and policies on legislative lobbying where a million dollars spent trying to change the rules of the game in one's own favor can at times improve a firm's profitability more than spending that million productively in renovating plant or increasing efficiency.

Currently, the primary locus of decisions in matters of distribution is the national community, even though local considerations are important and international discrepancies are so morally compelling that greater international co-ordination is necessary. Charitable, voluntary efforts are important at all levels, but the most basic need for a structure of justly distributed wealth is that embedded in the national economy. In a radically egalitarian commune, the primary goal related to distribution might be to increase income differentials to compensate individuals more fairly. In our context, the primary goal of those most concerned with this problem is clearly to reduce inequality.

Describing distribution as a separable problem has certain disadvantages, primarily because it might be argued to be a subset of the fourth problem, the quality of relations in the economy. Separating it out would seem to give it a greater importance than other issues related to the quality of relations which are in fact equally crucial. Still, economists (and the wider public) have traditionally acknowledged that distribution is a problem separate from allocation and one which the market is not well suited to solve. Thus, treating distribution as one of the four basic problems builds on an existing understanding that allocation, for all its importance, is but a part of the question.

Scale

The third problem is that of achieving the proper scale for the economy within the biosphere. This is a relatively new problem. There have been examples of pre-modern problems of scale, but these have been localized phenomena. The

cliff-dwelling Anasazi of what is now south-western Colorado flourished for several hundred years and then disappeared in a matter of decades in the early thirteenth century, probably because they over-taxed the environment in a period of drought. Similarly, citizens of the large industrial cities of England in the nineteenth century repeatedly experienced winters where the smoke from coal-stoked heaters all-too-often filled the air and their lungs. Still only in the last few decades have we become acutely aware of the limits of our biosphere as a storehouse for resources and a sink for wastes.

Fundamentally, of course, problems of world-wide scale are completely beyond the reach and ken of unconstrained individual economic activity. Economists have long known that the depletion of a common pool of oil or water will occur too fast if there is no coordination, either imposed by outsiders like government or possibly by the group of all who own rights to deplete the pool. Economists have similarly noted the existence of "externalities" or "neighborhood effects." These are either negative effects of economic actors felt by others where the costs are not paid by those causing them, or, in some cases, positive effects caused for others where those causing them cannot reap the benefits.

Still, such acknowledgments have been added on to the structure of orthodox economics as minor corrections, as Ptolemaic epicycles, without causing any major revision of the paradigm whose validity is weakened the more seriously externalities are taken. Clearly today, the problem of scale is not only real but immensely important. The greenhouse effect and depletion of the ozone layer are perhaps the two most pressing issues, but the list of problems is far longer: waste treatment and storage, resource depletion, etc. While some of these may be made more tractable by technological breakthrough, the point here is that treating the problem of allocation as if it were far and away prior to the problem of scale is shortsighted and foolhardy. As Herman Daly and John Cobb put it in the language familiar to economists, determining the appropriate scale for the economy is a distinct optimization problem, one that cannot be subsumed under the effort to achieve an allocative optimum.[38]

The general goal guiding responses to the problem of scale is sustainability. The time-frame for this sustainability is not easy to specify. While a thousand years is tempting, nearly everyone admits that technological change over that time will likely be unthinkably immense and that presumptions of zero or small technological change are ludicrous. A time-frame of a century may be more appropriate, but any line drawn here is clearly arbitrary.

The primary perceived evil when talking of scale is mindless, unsustainable growth. If world industrial production continues apace, serious climatic temperature shifts of even a few degrees Celsius could quite easily impose economic (not to mention human) costs that are both staggering and irreversible. If the production of energy continues to require more and more energy inputs to produce the same amount of energy to be sold (and this is likely as the more accessible sources of energy are consumed first in good economically rational fashion), petroleum may in the next five or six decades vanish altogether as a significant world energy source.[39]

Historians of the next century may shake their heads at what look like reasonable market decisions today, for these may appear as shortsighted choices based on a naive extrapolation of a two-hundred-year era of good fortune which in reality was built on the exhaustion of a resource base that took ten thousand times that long to create. Technological innovations may indeed come to the rescue for a time, as could happen if effective and cheap smokestack "scrubbers" made the world's coal resources less threatening, but that possibility only brings us round again to the limits established by the greenhouse effect. Fusion remains a hope, but a very uncertain one. Fundamentally, the problem of scale is an immense and intractable one for any modern economy.

The Quality of Human Relations

The fourth problem is that of the quality of human relations. This is without doubt the most complex of the four in that it is perhaps more accurately described as a complex of related problems. Still, as our purpose here is the development of a framework for thinking about the economy, many of the subtleties must be neglected; the general governing goal of this fourth problem of the quality of relations is to develop and sustain strong persons in active communities. This problem needs to be seen as integral to economic life (and not a peripheral concern attended to by the moral or cultural realms) because economic life generally, *as well as economic life considered narrowly as allocation,* is only possible to the extent that the individuals and communities involved are well constituted.

The primary values to be achieved under the heading of the quality of relations are individuality, creativity, community, and participation. The meaning of any one of these is widely debated and heavily influenced by a nation's culture and informal traditions, but clearly within the United States these include democracy, freedom, and accountability. The U.S. Catholic Bishops, for example, have tried to describe what these values should mean in some detail. The primary perceived evils within this fourth problem are polar opposites: the loss of the individual in the group and the loss of community as a result of individualism. The locus for decisions affecting this vitality of persons and communities is less focused than for any of the other three problems: The locus extends from individuals' decisions to those taken at any level of group interaction.

Any specification of the major goal to be accomplished in our current context will also be subject to diverse interpretations. I will, however, argue that two stand out: strengthening communal economic control at each level and limiting the psychic distance that threatens human relations in bureaucracy, primarily in bureaucratic government, but also in bureaucracy within large corporations, universities and other large human institutions. These two, of course, are themselves in tension, but together they mark the importance of responsive and robust channeling of economic activity. Note here that there are other and more

chronic objections to tendencies within bureaucracy, most notably that it can obstruct good allocation (the first problem), but it qualifies here as well because the rigidities and unresponsiveness that threaten bureaucracy in any environment are detrimental to individuals and community.

Negative Interactions Among Efforts to Address the Four Problems

This framework of four problems is designed simply to distinguish, organize, and relate the basic problems facing any modern economy. It cannot of itself resolve the truly critical questions about the relative importance of the four problems or the relative importance of the various values and goals implicit within each one. To take just one example, Robert Nozick and Michael Walzer have widely divergent views on the relation of individual and community, and the schematic framework I am developing here provides little, if any, help in adjudicating their differences. However, it is clear that if any serious attempt at adjudication is to be made, it will have to begin with a clear differentiation among the problems, and it will require that all four sets of issues be laid on the table. In current practice we find that some parties to the economic policy debate conveniently forget about three of the problems in their enthusiasm for solutions to one of them.

This forgetfulness is not difficult to understand. It is much harder to develop simple and satisfying solutions when all four problems are considered together. Compromises have to be made and costs have to be accepted. Some of the negative interactions between efforts to solve the different problems are outlined in Figure 2.

Let us begin by considering ways in which solutions to other problems can have an adverse impact on successful allocation. Actions oriented to improving distribution can impair production through a loss of incentive on the part of those receiving government transfer payments (whether the unemployed, farmers, or big business) or through a drop of savings and investment if taxes on these were raised dramatically to pay for redistribution.[40] The sort of controls needed for solving the problem of scale can easily lead to special interest distortions and bureaucratic blunders harmful to allocation. Efforts to improve the quality of relations in economic life often have significant costs for worthwhile changes (e.g., the cost of court systems to enforce contracts, the cost of education on the dangers of drugs or smoking, the cost of due process requirements within firms, etc.). In addition, what economists call special-interest distortions are always possible as individuals and groups seek gains for themselves under the banner of improving the quality of relations generally.

In the case of distribution, it is clear that actions oriented to improving allocation often and even generally have some effects at odds with the goals of distribution. Let us start with the ethicist's notion of "dessert", i.e., what is a

The Four Problems of Economic Life
Figure 2

Problems to be Resolved	Threats arising from the goals related to: Allocation	Distribution	Scale	Quality of Relations
Allocation		Loss of incentive Drop in savings/ investment	Special interest distortions Bureaucratic blunders	Increased costs in production Special interest distortions
Distribution	Equitable distribution is ignored by the market		Reductions in scale & in wealth make redistribution harder Special interest effects	Higher costs & lower wealth make redistribution harder
Scale	No internalization of social costs	Redistribution easier with growth		Higher cost & lower wealth make it harder to impose limits
Quality of Relations	Market undercuts communal ties and values	Mindless redistribution may erode individuality, families, customs & values	Heavy authority in national community Loss of freedom	

valid reason for *deserving* some of the goods and services produced in the nation. Some bases for dessert — need, for example — are entirely ineffective within the market. Other bases for dessert — like effort or risk — are indeed rewarded by the market but only the most doctrinaire marketeers or libertarians would assert that the market scheme is the morally optimal one for rewarding effort and risk. Goals related to the problem of scale can likewise threaten the general goal of equity in distribution, as when special interest effects (always oriented to the powerful not the poor) or environmentally necessary economic retrenchment leave fewer resources available for redistributive efforts. Similarly, attempts to improve the quality of relations would impair distributive efforts if higher costs of achieving some other goals diminished wealth, making redistribution harder, either economically or politically.

Efforts to solve the problem of scale are threatened by actions in service to allocation because individuals and institutions have economic incentives to ignore the social costs they cause. And because improvements in both distribution and the quality of relations are generally costly, and thus easier to accomplish with economic growth, efforts to solve these problems will often conflict with simultaneous efforts to solve the problem of scale.

Similarly, efforts to improve the quality of relations are threatened by pursuit of the goals related to the other problems. The tendency for the market to undercut communal ties and traditional values has been well documented and critiqued. Economist, such as Joseph Schumpeter[41] and Thorstein Veblen,[42] have even argued that this tendency in capitalism erodes the moral foundations on which markets must stand, thereby leading to the demise of capitalism itself. Similarly, some attempts to improve distribution (e.g., welfare rules that refuse benefits to two-parent families) may erode family ties, individuality, customs, etc. The strong national or international authorities that may be needed to address the problem of scale could entail the sort of restrictions on democratic freedoms feared by Robert Heilbroner in his *An Inquiry into the Human Prospect.*[43]

Positive Interactions Among Efforts to Address the Four Problems

At the same time, of course, solutions to these four problems are not mutually exclusive. Carefully conceived and implemented, efforts to address one problem can have positive effects on the others, as Figure 3 summarizes all too briefly.

The most important of these positive interactions are those between allocation and the latter three problems. I say "most important" because so much of recent neo-conservative writing on ethics and economics has been directed against those trying to address one of the other three problems; such arguments rest on the claim that other approaches threaten the production of goods and

The Four Problems of Economic Life
Figure 3

Problem to be Resolved	Support arising from: Greater Per Capita Wealth	Greater Equity	Greater Sustainability	Stronger Individuals & Communities
Allocation		Greater loyalty & motivation Better educated work force	Prevents unsustainable goals	Increased motivation & creativity Better educated work force
Distribution	Redistribution easier with wealth		Long-run improvements in equity more possible	Greater equity perceived as valuable
Scale	Necessary changes are more affordable	Greater willingness to sacrifice for sustainability		Greater willingness to sacrifice for sustainability
Quality of Relations	Improvements more affordable Creativity & individuality rewarded	Improvements more likely	Prevents dislocations of social crises	

services. As we have just seen, there are tradeoffs between and among these four basic goals, but the simplistic form of the argument heard so often takes an ahistorical view of production as somehow prior to the others and views those other goals as unidirectionally dependent on production. This argument goes on to endorse (more or less) the current state of social legislation but offers no justification of its implicit demand that we stop the development of social legislation at its current position and go no farther.

This argument is shortsighted. Efforts to improve distribution can indeed conduce to better productivity. In fact, without a broadly accepted conception of equity in a society, both workplace predictability and political stability are at risk. Efforts to improve distribution affect workplace loyalty and motivation and they enable lower-income citizens to become better educated and thereby better able to advance economically through productive contributions in the economy.

Steps to address scale are also crucial for allocation. Unless a sustainable economic process is established, impressive gains today may well look shortsighted and even foolhardy fifty years from now. When intergenerational equity is taken into consideration (and there are few morally weighty arguments for discounting the welfare of future generations as much as self-interest in the market does), sustainability moves from a prudent reasonableness to a moral obligation.

As important as the goals of equity and sustainability are for allocation, the goal of developing strong individuals and communities is even more critical. Neo-conservative defenders of the market system often praise the productive, wealth-producing capacity of capitalism as the engine providing the means for accomplishing other goals in life like equity or environmental improvements. However, it is certainly more accurate to say that it is the presence of strong, creative, and public-spirited individuals in strong, creative and caring communities and institutions that has made possible the dramatic advances in productivity within the market system. There is a network of human relationships on which is supported the individuality that makes the economy vibrant. The danger is that, as the rationality of the market tends to weaken the values and communal ties of this network, the individuality that fuels the market may burn too hot and consume the network necessary to support it.

For the same reasons that the quality of relations has been literally essential to our current prosperity, improvements in this quality can have still further positive effects on the allocative process. Economists engage in strenuous debates on this issue, of course, and I do not take my asserting such positive effects to be adequate argumentation for them. Nonetheless, I am convinced that stricter workplace safety standards, more aid to education (particularly for low-income groups), security from medical catastrophe, and many other particular goals related to improving the quality of relations would contribute to our national welfare and would have beneficial effects in production through increased motivation, better education, stronger personal and familial security from which market-oriented ingenuity and risk-taking arise.

Some neo-conservatives do explicitly praise the many historic steps taken through government action (social legislation) to humanize capitalism,[44] but nearly all of them oppose further steps in this direction. Peculiarly, however, there is almost always an asymmetry in their rationale. While they usually oppose further social legislation on the grounds that it would interfere with allocative efficiency, that could also be said (and was!) about the social legislation that they now take for granted. When an issue is one of tradeoffs between, say, allocation and the quality of relations, it is insufficient to consider only the benefits and costs within allocation. A responsible argument requires that benefits and costs within the quality of relations be carefully attended to as well.

While the positive interaction among the other permutations of these four problems are important, they are both less intricate and less controverted. Improving distribution is easier, other things being equal, with growth and is more difficult without it. While many efforts to improve sustainability compete for real resources with efforts to improve distribution, it is clear that long-run improvements in distribution require sustainable long-term economic prosperity. With the improvement of the vitality of individuals and communities comes a greater appreciation of the value of equity within the nation. The very possibility mentioned earlier of subsuming the goals of distribution under those of quality of relations speaks to the positive interaction of efforts to address these two problems.

The goals related to the problem of scale clearly conflict with the unencumbered operation of the market, but it is also true that environmentally necessary changes in production will be easier to make with rising per capita GNP, particularly if that growth is an environmentally benign sort. Advances in equity will probably bring about a greater willingness to sacrifice for sustainability, as will advances in the quality of individuals and communities.

While some of the goals related to the quality of relations are in critical ways threatened by the market, others, like creativity and individuality, are rewarded and encouraged.[45] And of course, improvements in productivity make it easier to afford expenditures to improve the quality of relations. Improvement in equity might be seen as a subset of improvements in the quality of relations, and a greater sense of equity can increase one's sense of self and of the importance of appropriate communal ties. Enhancements in sustainability benefit the quality of relations in that they serve to prevent the social dislocations which would surely follow upon environmentally induced economic crises.

Conclusion

In summary, then, the economic life of a nation can be thought of as entailing four separable problems: allocation, distribution, scale, and the quality of relations. The strength of the capitalist form of economic organization has been its unprecedented success in the allocation of resources in the market. Relying upon and rewarding self-interested activity of individuals and organizations has led to the greatest outburst of economic productivity in the history of humankind. As Bernard Mandeville put it nearly three centuries ago, the system is one where "the very Poor Lived better than the Rich before."[46]

From the point of view of Christian ethics and ethics more generally, this favorable consequence is significant and weighs heavily in favor of a generally free market. Still, there are negative effects of the system and these weigh heavily on the other side of the balance. Regardless of the balance, it must be admitted that the productive process, here referred to as allocation, is but one of the basic problems to be addressed in setting the rules of the game for economic life. Although self-interested activity deserves a endorsement within the process of allocation, the extrapolation of the legitimacy of self-interested behavior outside the allocation process cannot rely on arguments that it simply helps allocative efficiency. That is not the issue.

Neo-conservatives are owed a debt of gratitude for disclosing the moral foundations of capitalism and for reminding business practitioners and others of the importance of such foundations. Recognizing the many benefits of self-interest within markets may be difficult for some critics of the system. Critics on the left are owed a debt of gratitude as well -- for insisting on a more just distribution of income and wealth and for resisting attempts to extend self-interest pervasively. Recognizing the restricted nature of the legitimacy of self-interest may be difficult for some defenders of the system. Attempting to adjudicate the differences in opinion about the relative weights of the various goals in economic life will not be easy, but since we face multiple problems, it is critical to begin by recognizing vividly the tradeoffs that will have to be made.

NOTES

An earlier version of this argument appears in *The Annual of the Society of Christian Ethics: 1989.*

1 See, for example, Marvin Olasky, *Patterns of Corporate Philanthropy: Public Affairs Giving and the Forbes 100*, (Washington, D.C.: Capital Research Center). As Olasky puts it, "Limitation of government powers and an emphasis on property and family have underwritten the American success story. It would be both ironic and tragic for that success to be undermined by the very institutions that have grown our of, and contributed to, that success. . . " See "Landmark Study Documents American Corporate 'Killanthropy'," by Willa Ann Johnson, in *Imprimis*, (Hillsdale College, Hillsdale, MI) 17, no. 6 (June 1988): 6-7. See also Irving Kristol's "On Corporate Philanthropy," in *Two Cheers for Capitalism*, (New York: Basic Books, 1978), 131-35.

2 George Gilder, *Wealth and Poverty*, (New York: Basic Books, 1981), 36-37. We might note that Gilder's criticism of Smith occurs in the midst of a crass misreading of him. Gilder terms Smith's reliance on self-interest "a Faustian pact" and "a deal with the devil" as if Smith actually advocated vice as a worthwhile tradeoff for prosperity (Gilder, *Wealth and Poverty*, 36). On the contrary, Smith's view was that people do in fact tend to act out of self-interest and, with competition, this tendency can be both held in check and made productive for the general welfare.

3 ibid, 82.

4 ibid, 77.

5 Ian Hore-Lacy, *Creating Common Wealth*, (Sutherland, NSW: Albatross Books Pty. Ltd., 1985), 10. It should be noted that in spite of Hore-Lacy's somewhat limited view here, compared to many others writing to defend capitalism, he speaks for a stronger effort to offset the system's harsher effects.

6 Robert Benne, *The Ethic of Democratic Capitalism: A Moral Reassessment*, (Philadelphia: Fortress Press, 1981), 128.

7 Benne, *Ethic of Democratic Capitalism*, 135.

8 Michael Novak, *The Spirit of Democratic Capitalism*, (New York: American Enterprise Institute, 1982), 175. Similarly, Peter Berger attributes the breakdown of traditions in contemporary society not to capitalism but to "modernization," something equally important in socialist nations. While there is certainly some truth to this, it also lets capitalism off a widely agreed upon hook and it represents an astigmatism not easily excused in a sociologist. See Berger's *The Capitalist Revolution: Fifty Propositions about Prosperity, Equality, and Liberty*, (New York: Basic Books, 1986), 220-21.

9 Novak, *Spirit*, 92-95.

10 Novak, *Spirit*, 93.

11 Novak explicitly appeals to Smith's *Theory of Moral Sentiments* and the notion of objectivity in weighing one's own interests, Novak, Spirit, 95.

12 Michael Walzer, *Spheres of Justice: A Defense of Pluralism and Equality*, (New York: Basic Books, 1983), chapter 4.

13 For a helpful outline of the boundaries of these positions (and his own) see David Hollenbach, S.J., "Liberalism, Communitarianism, and the Bishops' Pastoral Letter on the Economy," *The Annual of the Society of Christian Ethics*, 1987, 19-40.

14 Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, (New York, Modern Library, 1937), book 1, chapter 2, 14.

15 Smith, *Wealth of Nations*, "Introduction and Plan of the Work," see also, book 2, chapter 2, where "gross revenue" is employed as equivalent to the term "wealth." It should be noted that Smith cast this within what is usually called a labor theory of value, but the difference between this perspective and that now dominant in mainstream economics today is not critical for the issue at hand.

16 Unlike economists today, Smith is unappreciative of those who provide only services. Readers may be shocked to learn that Smith grouped under "unproductive workers" many whom he simultaneously considered "honourable," "useful," or even "necessary," many in "noble professions," such as clergy, lawyers, physicians, entertainers, the military and the king himself (Smith, *Wealth of Nations*, book 2, chapter 3, 315). It will be no surprise that University professors do not escape the long reach of the adjective "unproductive." Of course, later economic practice came understandably to consider such service workers "productive," and even some service workers as contributing to the

nation's capital stock, but the point here is that for Smith the main economic goal was measured by annual national production, not by the aggregate possessions of the nation's citizens.

17 Not all commentators read Smith in this way. Some, like Schumpeter, simply translate such phrases as "the whole annual produce of its industry" [Smith, book 4, chapter 2, p. 423] into "material products that are useful and transferable and cost labor to acquire or produce." See Joseph Schumpeter, *History of Economic Analysis*, (New York: Oxford University Press, 1954), 626.

18 Smith, *Wealth of Nations* book 1, chapter 10, 128.

19 Joseph Cropsey, "The Invisible Hand: Moral and Political Considerations", in Gerald P. O'Driscoll, Jr., ed., *Adam Smith and Modern Political Economy: Bicentennial Essays on the Wealth of Nations*, (Ames, Iowa: The Iowa State University Press, 1979), 165-76.

20 ibid., 169.

21 ibid., 168-69.

22 Smith, *Wealth of Nations*, book 4, chapter 2, 421.

23 ibid.

24 According to Schumpeter (and Joseph Viner before him), Smith's view never got beyond the assertion that goods will be produced in that nation where their cost of production is lowest. See Joseph Schumpeter, *History of Economic Analysis*, (New York: Oxford University Press, 1954), 607.

25 David Ricardo, *The Principles of Political Economy and Taxation*, third edition, 1821, (London: J.M. Dent and Sons, Ltd., 1911), 82ff. Subtleties inherent in the relative costs of the two goods in the two nations and in what economists call the "terms of trade" are not important for our purposes here. Any standard intermediate microeconomic theory textbook will address these.

26 I am indebted to John Cobb and Herman Daly for this insight into Ricardo's classic text. See their forthcoming book, *For the Common Good*, (Boston: Beacon Press, 1989).

27 Ricardo, *Principles*, 83.

28 ibid.

29 ibid.

30 John Stuart Mill, *A System of Logic, Ratiocinative and Inductive*, 2, (London: Longmans, Green, Reader, and Dyer, 1875), book 4, chapter 12, section 6, 554. See also his "On the Definition of Political Economy; and on the Method of Investigation Proper to It," in *Essays on Some Unsettled Questions of Political Economy*, second ed. 1874, reprinted, (Clifton, N.J.: Augustus M. Kelley, 1974), 119-64.

31 Amartya Sen, *On Ethics and Economics*, (New York: Basil Blackwell, 1987), 80-88. See also Sen, "Goals, Commitment and Identity," *Journal of Law, Economics and Organization*, 1 (Fall 1985): 341-55.

32 Sen, *On Ethics and Economics*, 81.

33 Much thought is being put to revitalizing the economist's view of self-interest. See, for example, Albert O. Hirschman, "Against Parsimony: Three Easy Ways of Complicating Some Categories of Economic Discourse," *American Economic Review*, 70, no. 2 (May 1984): 89-96. Some economists have moved to a more or less socio-biological argument that some forms of virtuous activity may be economically advantageous (because trading partners can expect to be treated fairly) with the result that it might be in the self-interest of a person to choose not to be self-interested. In good and sequacious socio-biological form, such virtuous persons might thrive over the ages while more narrowly self-interested behaviors might be extinguished. See Robert H. Frank, "If *Homo Economicus* Could Choose His Own Utility Function, Would He Want One with a Conscience?" *American Economic Review*, 77, no. 4 (September, 1987): 593-604.

34 James Boyd White, "Economics and Law: Two Cultures in Tension," *Tennessee Law Review*, 54, no. 2 (Winter 1987): 192.

35 Lay Commission on Catholic Social Teaching and the U.S. Economy, *Toward the Future: Catholic Social Teaching and the U.S. Economy*, (New York, Lay Commission, 1984), 39. As unhelpful as this definition is, another appearing earlier in the text is even less so, where "self-interest rightly understood" is taken to mean "that self-interest which reaches out to embrace the interests of others, near and far," 24.

36 Perhaps the best example of this is Gary Becker. See, for example, his *The Economic Approach to Human Behavior*, (Chicago: University of Chicago Press, 1976).

37 There is always a problem in deciding whether and by how much "wealth" changes from year to year. The usual measure is the Gross National Product (GNP), but it has many limitations as a measure for economic welfare. The treatment of allocation here ignores difficulties in any definition of what counts for "improvement," thereby leaving some quite important issues unattended to.

38 Cobb and Daly, *For the Common Good.*

39 See, for example, *Beyond Oil: The Threat to Food and Fuel in the Coming Decades*, J. Gever, R. Kaufmann, D. Skole and C. Vorosmarty, (Cambridge, MA: Ballinger Publishing Co., 1986), especially chapter 2.

40 Of course, simply crying wolf here is no proof that the wolf is near. In spite of Reagan era assertions that tax reductions for the wealthy would be the key to investment and an end to the major recession of the early 1980's, most economists now agree that consumer spending and not a rise in tax-induced investment brought the end to the recession, a very Keynesian solution and not a supply-side one.

41 Schumpeter, *Capitalism, Socialism and Democracy*, (New York: Harper, 1942).

42 Thorstein Veblen, *The Theory of Business Enterprise*, (New York: New American Library, 1958). See especially chapter 10, "The Natural Decay of Business Enterprise."

43 Robert Heilbroner, *An Inquiry into the Human Prospect*, (New York: Norton, 1974).

44 For example, Novak refers favorably to labor unions, the forty hour work-week, child labor laws, and social security in *The Spirit of Democratic Capitalism*, 47. Missing, however, is any criterion to distinguish these appropriate developments from other humanizing proposals today of which he would not approve.

45 Few commentators have spoken so strongly about the positive effects of economic growth on the quality of persons and communities as has Michael Novak. See, for example, *Spirit of Democratic Capitalism*, 15-6.

46 Bernard Mandeville, "The Grumbling Hive: or Knaves Turn'd Honest," in *The Fable of the Bees*, ed., Philip Harth, (London: Penguin, 1970), 69.

The Clemens Lecture Series

Self-Interest, Markets, and the Four Problems of Economic Life

Daniel Rush Finn, Ph.D.

The Clemens Chair in Economics and the Liberal Arts and the Clemens Lecture Series have been made possible by the generous gift of William E. and Virginia Clemens. William Clemens, an alumnus of Saint John's, is the founder and president of Bankers Systems, Inc., of St. Cloud. The firm, founded in 1952, employs more than 600 persons. Bankers Systems designs and produces supplies for financial institutions. The Clemens have four children, Barb, Mary Sue, Robin and John.

One of the purposes of the Chair and the Series is to achieve an increase in the interdisciplinary exchange between economics and other liberal arts disciplines.

For additional copies of the lectures write to: Mary Wilson, Clemens Chair, Saint John's University, Collegeville, MN 56321.