

## CHAPTER 1

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### In Praise of Dissent

#### Discontent and Discourse

By most counts, the world is a better place today than it was in ancient times. First and foremost, we have the comforts that come from our greater collective wealth. But even apart from that, we do not live in perpetual fear that another nation's marauding army will come and take away our land and belongings. When we return home from dining out, we do not expect to find that strangers have broken in and occupied our homes. The physically weak do not have to be reconciled to being economically destitute. There are numerous rights of individuals and nations that are presently treated as fundamental and inviolable. We do not have to be on constant guard to defend these rights by force or guile. Others recognize the rights and usually respect them, and when they do not, the community or the state usually enforces them.

It would be a tortuous claim to say that we are not, on average, more fortunate than our ancestors. It will be argued in this book, however, that we are not as fortunate as may appear at first sight. The fact that the exploitation of the twenty-first century occurs within the laws and norms of the twenty-first century should not make us oblivious to it. Even in ancient times, what appear to us today as brutal, confrontational behaviors and morally indefensible conquests were more often than not justified using the morals, norms, and practices of the times. When Plato or, closer to our time, Thomas More wrote about a utopian society in which all men were treated well and with dignity, it did not even occur to them that there might be something wrong in leaving women and slaves out of this scheme. When during the seventeenth, eighteenth, and nineteenth centuries Native Americans were systematically separated from their land, occasionally by force but frequently by what on the face of it looked like voluntary transactions—elaborate contracts that the Native Americans usually did not understand, since prior to the arrival of the Europeans they had neither experience of land trade nor written contracts<sup>1</sup>—they were being exploited quite ruthlessly, as their subsequent impoverishment suggests. But it

was widely believed that what was happening was lawful and morally justified (Banner 2005, especially 52–53; see also Robertson 2005).

Some accounts of these “voluntary” treaties and contracts are tragic, such as when in 1755 in South Carolina more than five hundred Cherokee met with a similar number of settlers. South Carolina Governor James Glen convened the meeting. Gifts were exchanged, and meals were served in silver bowls and cups. The Cherokee were pleased, and declared that the tribe wished to give “all their Lands to the King of Great Britain ... for they acknowledge him to be the owner of all their Lands and Waters” (Banner 2005, 59). The settlers sensed that this was a metaphoric use of language, just a way of being nice to outsiders.<sup>2</sup> This was especially clear when the Cherokee refused to take any payment for their offer. But the offer was too good for the settlers to allow qualms about metaphoric speech to get in the way. To make it into a contract, the settlers persuaded the Cherokee to take a small payment, which they accepted out of politeness. Little did the Cherokee realize that they were about to lose all their land.

At one level, deals like the above one were voluntary, but the question must arise about the meaning and significance of voluntary contracts between two parties when one of them does not understand what a land sale means because it has not had any experience of that in its history. Many of the settlers considered the deals to be fair, and so did many of the natives, though of course there were settlers who were out to take ruthless advantage of the simplicity of the natives. When Christopher Columbus and his crew landed in what is now the United States (Bahamas), the Arawaks ran to greet them with food and gifts. They had no idea that Columbus viewed the whole situation as an opportunity. In Columbus’s own words, “They brought us parrots and balls of cotton ... and many other things.... They do not bear arms and do not know them for I showed them a sword, they took it by the edge and cut themselves.” And having noted the simplicity of these people, he went on to observe that “they would make fine servants. With fifty men we could subjugate them all and make them do whatever we want” (Zinn 2003, 1).

Likewise today, when we see the rule of law prevail, property rights as defined by our courts respected, and blatant military conquests decrease in number, we feel that what we see happening in the marketplace and our conference rooms where treaties and agreements are signed is the outcome of fair play. We know that people get cheated in markets and that individuals do get exploited, but overall, when we play by the rules of the market and do not snatch and rob, we believe we are on the right path. Some do get impoverished and some get rich. Well, we tell ourselves, this has to happen, does it not? Would trying to halt this not impede progress and economic growth? We

have seen—for instance, in the Soviet Union—what happens when other systems are attempted. But history, such as the cases just discussed, should alert us that even today, there may well be other kinds of unfair contracts and treaties taking place. After all, the exchanges that happen in reality are not just of apples, haircuts, guns, and butter with money, as our textbooks suggest, but complex deals involving long stretches of the future and complicated rights. It is likely that groups are being outwitted in novel ways that will become clear to us only in retrospect.

It is arguable that if we measure inequality simply by the income gap between the richest and poorest segments of society, then the present-day world has inequality at a level that has never occurred in human history.<sup>3</sup> This is because the poorest people's condition has remained much the same from ancient times. Their lives are nasty, brutish, and short—to use an abbreviated version of Thomas Hobbes's famous description of life in the state of nature; the poorest people barely get enough to survive. Their well-being is usually determined by the biological subsistence needs of human beings. Even poorer people will not be around to be counted. Wealth, on the other hand, has no natural ceiling. The richest people today can do things that neither Genghis Khan nor Nero could even dream of.

It can be shown by some simple back-of-the-envelope calculations that the ten richest people in the contemporary world together earn the same income as is earned by the entire population—close to forty million people—of Tanzania (Basu 2006b). Given that Tanzania has its own share of millionaires and the super rich, it is obvious that if we leave such people out and compare the ten richest people with the poorest people in the world, we would find a gap that should be mind-boggling. What is shocking is that it does not boggle our minds. We usually do not think about these matters, and when we do, for the most part we treat the inequality and poverty as inevitable concomitants of the market system—that grand, invisible machine that coordinates millions of participants in this huge global system, creates efficiency, and helps the world grow richer.

Intracorporation inequality has been rising exponentially. In the United States, the average pay of the CEOs of large corporations used to be forty times that of the average production worker in 1980. Ten years later the ratio had climbed to eighty-five, and at the start of the twenty-first century the ratio had risen to four hundred.<sup>4</sup> We have been persuaded to believe that a CEO who earns ten million dollars a year (not an implausible figure when the stock options are added to the base salary) needs that as *incentive* for their high-skilled job. The presumption is that in case the pay per unit of time for all executives was halved, so that the above CEOs now earned five million dollars a year,

they would say, “With such low compensation I will not work hard anymore.” It is a sign of our remarkable gullibility and complacency that we buy such arguments.<sup>5</sup> I have tried to demonstrate by constructing a formal model (Basu 2010a) how through the clever design of salaries and benefits, it is possible to create a situation whereby pay can vastly exceed productivity. Quite apart from the inequity of this, it creates a world prone to financial crashes, as witnessed during 2007–9.

The complacency that prevails in our societies in the face of such inequity is not altogether spontaneous, though. It is propped up by a large number of people who benefit from the system. These people are a minority of the world’s population, but one that matters; it consists of those who have a voice and can make themselves heard, either by paying to have their opinion fed into our laws and regulatory systems, or by being better networked and better embedded in the citadels of power.

This is known to all but the most gullible. Yet the complacency also has another prop. It is made possible by legions of economists, plying their daily trades—writing their monthly columns, publishing their annual papers, and putting out their decadal books. This has created a ‘central opinion’: a body of intellectual material that describes how a modern economy functions, and assures us that as a system, the current world economic order, founded on individual selfishness and the ‘invisible hand’ of the free market, is right or, at any rate, the best among what is feasible. It may not always function as it should but as an ideal, it is the right one to pursue and uphold.

When I distance myself from mainstream economics, I am aware that there are contemporary economists who share my concerns and would have no problem with my critiques. I am happily reconciled to the fact that the book’s novelty value will be limited for them. Nevertheless aided by a majority of practicing economists and economic journalists, the profession’s central tendency remains wedded to the view that the current world economic order as supported by the market economy of the industrialized nations is the only viable one not just for now but also in all conceivable futures. Our only task is to implement reforms to keep the existing system well oiled and humming.

Occasionally, this complacency gets ruffled. Bewildered by the depth of poverty and riches like never seen before, some people—including some who may themselves be privileged but have the courage to question—feel troubled. They wonder, Are we being duped into thinking that we have hit on the ideal system, our only task being to keep the system functioning smoothly? Anger builds up among these people, and it occasionally erupts in violence or unruly protests, in Saigon, Santiago, Seattle, or the streets of Washington, DC.

When those who have long been trod on and those who have empathy for them eventually decide to protest, their actions are often seen as the 'rampages' of 'marauding mobs.' But the inchoate suspicion that these protesters have felt about the existing world economic order is not entirely without justification. They may have failed to articulate their point of view, and their suspicions may have found expressions that appear pathological to the outsider, but their feelings hide an important truth that can be given intellectual foundations.

That is the reason for this book. Exploitation, conquest, and property grabbing are alive and well. The manner in which these practices occur has changed. Just as the modern world tries to plug the loopholes of blatant exploitation, and strives to halt plunder and egregious violations of basic human rights, human beings and governments discover newer and less obvious ways of exploiting the simple, the innocent, and the less materialistic. Whole nations, groups, and masses of people are being continuously outwitted and impoverished, not, or rather rarely, through wars and direct confrontation, but through complex financial maneuvers, the discovery of loopholes in the law, and the new opportunities that economic globalization opens up and the lagging process of social and political globalization leaves vulnerable to plunder. The decimated economies of sub-Saharan Africa, parts of Central and South America and Asia, and even some regions of Europe bear testimony to this.

One does not always have to go to faraway poor countries to discover the exploited or the outwitted. Even rich nations have large numbers of poor people and the destitute, who sleep in the streets (Jencks 1994; O'Flaherty 1996). As I write this, over forty million people in the United States live with no medical insurance, and close to 10 percent of the nation's labor force is unemployed.

Some of these poor people are no doubt less productive than the rich. But one can argue that being less productive should not be deemed reason to be cast into destitution and extreme poverty. Just as most of us would agree that being handicapped should not be a reason for being denied access to cinemas, restaurants, and shopping complexes, and hence we have laws that require public places to have special provisions for the handicapped, it could be contended that being less productive should not be a reason for suffering food deprivation and being denied medical help.

Even if we dismiss this line and go with the neoclassic assertion that it is fine for people to earn according to their productivity (and that is what makes an economy function efficiently), the truth is that the poor people of rich nations are not invariably or even typically the less productive ones. There is, for instance, overwhelming evidence that being born into wealth helps

one to be wealthy. Human capital acquired by going to elite schools and real capital transmitted from one generation to another through the legal protection of inheritance enables people *born into* advantage or disadvantage to remain that way, akin to what happens in caste-based societies. Further, people often fail to earn what would be prescribed by their productivity because they are outwitted of their wealth through the use of ever-more sophisticated financial contracts and exchanges.<sup>6</sup> This can create an ‘undeserving underclass’ in rich countries.

All this is kept from coming to a boil through a continuous ideological barrage of written and other media articulation of two myths: that an industrialized nation’s markets are free, and that free markets are fair. The legions of economists who dismiss the protesters in the streets of Seattle, Cancun, and Washington, DC, out of court are like those missionaries who accompanied the occupying armies of yesteryears, pacifying rebellion through comforting words, and ignoring the demurrers as misguided and befuddled. As Albert Einstein (1949, 9) wrote in the inaugural issue of *Monthly Review*, “The priests, in control of education, made the class division of society into a permanent institution and created a system of values by which the people were thenceforth, to a large extent unconsciously, guided in their social behavior.”

It is not being suggested that all this is happening through some conspiracy of the powerful and the rich. The world has fewer conspiracies than most people believe. There are conspiracies to be sure, but the force of unwitting atomistic action is usually far greater than we realize and in the end becomes the overwhelming force. And this is the force that is difficult to understand and needs serious intellectual inquiry to master. Adam Smith was right about this, and we must hold on to this wisdom even when we reject what in this book I refer to as Smith’s myth. What has to be kept in mind is that the absence of a conspiracy does not invariably make the equilibrium that prevails in society benign.

There is another view of the invisible hand that shares with Smith the idea that systems can run on their own steam, with no ultimate authority in charge, but the outcome is more malevolent and, on occasion, chilling. This is the vision of Franz Kafka, as immortalized in his unfinished novel, *The Trial*. Joseph K is caught in a surreal world where he is charged with a crime that he has not committed, and he does not fully understand the basis of the charge. He runs from pillar to post, from minion to minor bureaucrat, to find out what the charge is and who has handed it down, so that he can appeal his innocence. But in the society that K inhabits, there is no central authority or person to appeal to. All individuals in this labyrinthine world go about their limited daily chores, and this gives rise to forces that transcend each individ-

ual. In some ways, Kafka's view of our society is more pertinent than Smith's. It is true that Smith had scientific precision in his writing, while Kafka had all the ambiguities of a litterateur. Yet in social analysis, there is at times a need for the latter, and for meanings and messages to be conveyed through a deliberate use of ambiguity.

The state of our thinking on the global economic order that breeds complacency has intellectual roots that are deep and need to be excised carefully. That is the aim of this book. It is written in praise of dissent.

I should warn my readers at the outset, however, that many of them will be disappointed by this book, for it offers no panacea and has little of the edge of optimism one finds in revolutionary tracts. The aim is simply to hold a light up to society, and show that social and economic processes are not what we make them out to be. They are more venal than what the textbooks of economics suggest. The world is poised on a dangerous ledge. There is a risk that we will go headlong into a mean, materialistic future. What may disappoint some readers is my view that maybe, that is our future. Unlike most radical monographs, this book offers no compelling reason to believe that we will be able to avert this dismal predicament. At the same time, I hope that clarity in seeing the world as it actually is may enable us to think of ways to steer clear from such a future. I do offer some prescriptions and suggest new policy initiatives, but am aware that these may not measure up to the task. My central aim here is to lend clarity and be relentless about that, with the hope that someone more capable will provide the solution.

Another disappointment for some readers will be the eclectic methodology that is used here. For one, I critique mainstream economics but use many of its methods of analysis. For some it may seem that a natural instrument for a radical critique of the mainstream is Marxian economics. But the poor record of Marxian methods to dislodge neoclassical economics is a good warning sign. While I find Karl Marx's utopian constructions and normative yearnings attractive, as scientific method Marxian economics has little appeal to me. The search for, and more alarmingly, discovery of, empirical regularities over large swathes of human history is inevitably flawed. While I believe in determinism, which implies that the future that stretches in front of us is foretold, and as unalterable and free of chance as the history that lies behind us, I see no way that we can ever discover the trend that will unfold over the long run.<sup>7</sup> There may well be laws that an economy follows in the long run, yet claims of discovery of those laws appear to me, for the most part, delusional. It is one thing for something to exist, and quite another for it to be discovered or even be discoverable.

Moreover, while many contemporary Marxist thinkers have laudable normative aims—of a society that is more equitable and free from poverty—and

rightly refuse to accept the present distribution of wealth and income as fair, their positive analysis has been marred by a precommitment to certain set ideas about how society works. True radical thought requires us to be more open to new facts and newly discovered ways of reasoning. My strategy in this book is to pick the best available methods of reasoning, unmindful of where they come from. It so happens that much of the method used here has its roots in Smith's work. The fact that so much of mainstream economics can be laid to waste using its own instruments of analysis makes the critique that much more compelling.

To sum up, there is a large body of opinion that treats the current economic order, based on the pursuit of individual self-interest and untrammelled free markets, as the only viable one. It is argued in this book that all economic systems rely on social norms and beliefs. Much of the economics profession has taken the norms of capitalism so much for granted that these have, over time, become invisible and created the illusion of there being no norms. In truth, capitalism would collapse without its attendant norms.

This suggests that a more equitable and fair society than the one we currently inhabit is viable. There can be structures of norms and institutions that bring individual behavior into alignment with such a society. The design of such a system, and an understanding of its attendant norms and institutions, will not be an easy task both because this entails venturing into totally new areas of research and because those with a vested interest in the present system—that is, those who control most of the wealth of the world—will resist change and sabotage attempts to create a more equitable society. The aim of this book is to lay out the intellectual road map for this challenging project and develop a grammar for dissent.

This program of research and action gives rise to an important conundrum. It recognizes that piecemeal efforts for change and the adoption of idealistic policies, *as if* we already inhabit a utopian world, may well make matters worse. The failure to recognize this is a common mistake that some radicals have made. As long as we continue under the present system, we may have to live with conventional policies. For this reason, the message here must not be confused with the argument for a large government that some have proposed. A large government, in the current economic order, is a sitting duck. Large corporations and vested interests know that capturing this is a single-window access to profits. It is for this reason that many private firms consider the state to be the best business partner; they can, in the present system, fleece it for their own gains. The big versus small government debate is a misleading one, and it detracts from the larger aim of a more equitable world. The latter will be met with resistance from those who have vested interests in the current

regime, and to ensure that in the name of creating a better world we do not simply create another regime with a new oligarchy of interests will require a huge amount of intellectual effort.

What we have to realize is that prescribing standard (but intelligent) economic policies for the current regime and working toward a regime change are not inconsistent objectives. Indeed, both these underlie the project that is this book.

### Smith's Myth

The central opinion of economics has its origins in Smith's remarkable discovery that the order that we see in the world needs no central coordinator. The bread arriving on our dining table, the baker being supplied wheat by the farmer, and the farmer getting their seeds and fertilizer from the merchant can all be explained with no reference to a central coordinator or some benevolent conspiracy. Or to draw from Smith's most quoted line ([1776] 1937, 14), "It is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own interest."<sup>8</sup> Each individual serving his or her own interest can keep an economy brimming with activity and thus growing. An outsider viewing a modern economy, with goods changing hands and workers toiling away to produce goods in which they themselves have no interest, may be tempted to think that there is an outside agency or divine will that organizes this huge machinery. But Smith argued that this is not the case; the market is like an invisible hand that can guide producers and have goods delivered where they are most needed.<sup>9</sup>

The same view of the central opinion in mainstream economics was described more eloquently by the British Marxist economist Joan Robinson (1979, 43), in a commencement speech at the University of Maine in May 1977: "The philosophy of orthodox economics is that the pursuit of self-interest will lead to the benefit of society. By this means the moral problem is abolished. The moral problem is concerned with the conflict between individual interest and the interest of society. And this doctrine tells us that there is no conflict, we can all pursue our self-interest with a good conscience.... This doctrine is attributed to Adam Smith."

In case Smith's discovery seems obvious to us now, it is sobering to recall that the theory of the invisible hand would remain a conjecture for close to two centuries after the appearance of his classic, *An Inquiry into the Nature and Causes of the Wealth of Nations*, despite the copious writings by Smith himself and his successors in political economy. It took a considerable machinery of

mathematical economics, and the research of Kenneth Arrow, Gerard Debreu, Lionel Mackenzie and others, for it to be given formal shape and proof. It was well into the twentieth century that the conditions under which a competitive equilibrium exists and is optimal were formally demonstrated. That is, it was formally proved that, given some condition, all individuals pursuing their respective self-interest leads society to an optimal state. This has come to be known as the First Fundamental Theorem of Welfare Economics and is the formal statement of the invisible hand conjecture. I shall here refer to the Fundamental Theorem more colloquially as the ‘Invisible Hand Theorem.’ The terms used in the theorem, such as competition and optimality, belong to the jargon of modern economics, and as such have technical meanings. These are clarified in chapter 2, where the theorem is elaborated on.

This stateless, godless view of the world, as Smith’s theorem implied, shook the foundations of social thought in the eighteenth and nineteenth centuries.<sup>10</sup> It was a truly great idea.<sup>11</sup> But as with so many great ideas, some people worked to subvert it and others worked to modify its popular understanding to serve their own interests. In any case, it soon became the dominant idea, and from then on Smith’s *The Wealth of Nations* became the new orthodoxy.

As with religious texts, masses of people latched on to the orthodoxy with no further thought and no desire to question it, and without even the desire to read Smith further for fear that his ifs, buts, and provisos (and there were many of those in Smith’s writings) might dilute their conviction.<sup>12</sup> Smith’s great insight gradually ossified into a hard and unbending doctrine, which is referred to here as Smith’s myth. The “myth” referred not to what Smith wrote but rather to the way that his writings have come to be interpreted in popular perception. Regrettably, all the qualifiers and the warnings that Smith had sounded fell by the wayside. It is surprising to most contemporary economists who have not read *The Wealth of Nations* to learn that the invisible hand theory is not as central to Smith as it is made out to be.<sup>13</sup> Smith was much more critically concerned about economies of scale in the labor market, and the consequences of increasing returns for an economy’s growth and overall development. In fact, in the original index of his book there was no entry for invisible hand—this was later added by an editor when another edition appeared after Smith’s death.

It was not just Smith; several classical economists, notably John Stuart Mill and John McCulloch, took a more sophisticated view of the role of the market than the orthodoxy suggested. When some of these economists, including Smith, critiqued the state, part of the critique was an attack on mercantilism, and in particular, stemmed from the apprehension that the state

would be captured by the merchant class and thus be subservient only to its interest (see O'Brien 1975).

In spite of these exceptions, the orthodoxy thrived. In debates in the nineteenth century on setting statutory limits on the hours of work, people would flag Smith. If workers offered themselves for fourteen hours of work each day and entrepreneurs were willing to pay them for that, why should the state get into it? The invisible hand of the market would ensure that this 'natural state' was optimal. If women agreed to work for a wage less than what men got and firms were willing to hire women and men on those terms, why should the state get into it? If poor people offered themselves to a landlord to work as slaves and the landlord found the offer acceptable, then should the market not be left free to allow such a contract? These questions are not academic constructs but were instead matters of actual policy and debate. For instance, in 1859, the state of Louisiana declared voluntary slavery or what is often called 'waranteeism' to be legal.<sup>14</sup> That is, individuals were granted the right to become slaves. The law was, some would say, discriminatory because it granted this generous right only to persons of color.

It was argued that the state's involvement in all these matters would violate Smith's doctrine and be socially suboptimal. The fallacy in this assertion will be discussed in chapter 7.

So deep was this conviction that when the Invisible Hand Theorem was formally established in the mid-twentieth century, most economists treated this as a mathematical vindication of the belief. Even today, many economists equate the Invisible Hand Theorem with the normative proposition that we should leave individuals free to pursue their own selfish ends without any restraint. David Hume's famous warning about the fallacy of trying to get to normative propositions from purely positive axioms has been wantonly overlooked. The usual qualifiers—such as, there must be no negative externality associated with a person's own pursuits—are of course recognized by economists. But little beyond these minor caveats is acknowledged.

## The Lay of the Land

Since so much of the central opinion in economics relies on the Fundamental Theorem or, more accurately, misunderstanding the Fundamental Theorem, it is important for the reader to invest some effort to understand it. Hence, the next chapter begins with this and shows how much of contemporary popular thinking on economic policymaking is rooted in this theorem—or again, to state this more carefully, in a misreading of this theorem. This chapter covers

little fresh ground for trained economists, so they may wish to skip or skim through it. (But be warned that there are more people who think of themselves as trained economists than there actually are trained economists.)

There are many well-known critiques of why the theorem must not be taken to the real world too hastily for application. Those standard critiques are not of much concern to the present book; they are invoked only rarely. But for reasons of completeness and also to spare the subsequent chapters of interruptions to explain what is known, these critiques are also discussed in chapter 2.

The project of this monograph begins after that. The ultimate aim is ambitious: to show that the wisdom that was given to us by Smith has ossified into an ideology, which has hurt our understanding of how economies function, why some economies fail, and the role of markets and policy interventions. And these revisions, in turn, urge us to discard our complacency about the current world economic order. The conservative's dismissal of all other systems as 'incentive incompatible' and therefore not viable is a ruse, often unwittingly carried out, to sustain the vested interests of the current order. I will have occasion later in the book to study the true implications and meaning of incentive compatibility. The last chapters of this book will argue that global democracy is on the retreat and being continuously subverted by the powerful, and thanks to the marginalization of large sections of the world that is occurring concurrently with globalization, the world is headed into uncharted political waters, marked by turbulence. At an intuitive level, this is known by the laity. Yet this awareness has not transformed into policy, because of the economists' *modeled* world in which the market always delivers. As long as interventions are kept to a minimum, and the externalities are corrected with taxes and subsidies, the system is fair, all workers earning what is their marginal productivity. The fact that state-of-the-art journal papers have moved away from such a world has little effect on this 'central tendency' of the profession, and its penumbra of journalists, technocrats, and international civil servants. Moreover, the journal papers tend to marginalize themselves by being obsessed with the technical and mathematical criticisms.

There are more fundamental criticisms possible, which enable us to view the dismal conclusions of this book as compatible with and even a consequence of economic theory, thereby making it unnecessary to go into a denial of reality. And so the interim chapters—from 3 to 8—attempt to criticize and reconstruct the central model of economics. Chapter 3 discusses some deep flaws in our understanding and interpretation of the Invisible Hand Theorem. These criticisms are mathematically easy but conceptually hard. They suggest new axioms for economic theorizing. Chapters 4 to 7 demonstrate how these revised axioms result in an altered view as well as a deeper understanding of

how an economy functions and the role of policy interventions. In addition, these chapters maintain that economic theory needs to move away from its unquestioning adherence to methodological individualism. Chapter 8 carries these arguments over to the domain of globalization and international policy, and sets the ground for an analysis of global democracy and its erosion in chapter 9. The last chapter is a speculative one on how we could try to alter the current economic order, ranging from minor, relatively easy policy interventions to more radical and futuristic suggestions.

Before venturing into all of this, I want to sound a warning on understanding. What does it mean to *understand* how an economy works? It is important to answer this question, since much of this book is meant to be a contribution to our ‘understanding’ of how an economy functions, and how it interacts with society and politics, and it is hoped that the learning will occur at a level deeper than getting to know facts and mastering theorems.

## On Understanding

When I say the aim of this book is to create a deeper understanding of how an economy functions, I mean this in a somewhat unusual sense. There are at least two different senses in which we popularly use the term understanding. When people say that they “understand general equilibrium theory or Brouwer’s fixed point theorem,” and when they say that they “understand music or human psychology,” in both cases they are referring to cognitive processes in the brain, leading to some acquisition of information, but in different ways. The former refers to a ‘technical understanding,’ an ability to reproduce what one understands, and maybe even extend and modify what one understands. On the other hand, when people say that they understand music, this refers to an ‘intuitive understanding.’<sup>15</sup> This understanding is difficult to demonstrate to an outsider. (This is one reason that it is safe to claim that you understand music or art even if you do not.) But in some ways it is a deeper understanding. Consider a mentally challenged child. The trained psychologist will understand the child, but the child’s parent or sibling, with no training in psychology, may also make the same claim. However, the former’s understanding will be closer to what is called technical understanding above, and the latter’s understanding will be more intuitive. In many cases, the latter will have a better sense of what the child seeks and how the child will respond to certain stimuli. The parents or siblings may not be able to explain how they get to this understanding and so may not be able to impart this understanding to another person, but most people who have dealt with such situations will easily agree

that parents or siblings do have a kind of understanding that is different and in some ways deeper than that of the professional psychologist. It should be stressed here that it is not as if intuitive understanding cannot be enhanced through training. It can, and further, it can be more potent when combined with some technical understanding. People can learn to intuit better.

In most formal disciplines, we rely primarily on professionals with their technical knowledge. How good or bad this knowledge is depends on the discipline. For an automobile engineer, a good technical understanding may be adequate, or virtually so. My view is that in economics, the need for intuitive understanding is much greater than most economists would have you believe. Good economic policy requires a ‘feel’ for things over and above the knowledge of theorems and regression coefficients, just as one cannot be a good entrepreneur or a skilled driver merely by learning the techniques of management and innovation, or learning how the hand and foot movements of a driver translate into the maneuverings of a car. Though this may sound paradoxical, there are formal reasons for the need for intuitive understanding. It is an important part of this project to explain why this may be so.

For a full comprehension of this book, it is crucial to understand the material presented here *intuitively*. Hence, the style of writing in this book differs greatly from the standard text in economics. *Beyond the Invisible Hand* does not merely catalog results but also tries to construct a viewpoint by using reasoning, citing real-world examples, and most important, urging introspection. Moreover, in understanding what is presented here, there is some unlearning involved. People who have learned a lot of theory develop an incapacity to view the world as it really is. This does not have to happen—some of the most enlightened contemporary writers are also fine theorists—but it often does.<sup>16</sup> Textbook assumptions and axioms tend to crowd out other forms of learning, especially that which we learn from our daily experience. In some cases people who have learned a lot of theory do try to also learn from real life, but thanks to the distortion in their lenses caused by excessive learning, what they see merely confirms the presumptions that they have already formed.

This is not surprising in light of the research that has occurred on “confirmatory bias” (see Rabin and Shrag 1999)—that is, the propensity in human beings endowed with some initial opinion to find confirmation of that view in new information that is provided to them. Two persons with right-wing and left-wing views, respectively, exposed to the same set of new world events, would typically find reason to be even more convinced of their right and left wingness. In a fascinating experiment on this (Bruner and Potter 1964), a group of persons was shown a picture on a screen that was severely blurred and then gradually brought into focus, though it was never brought into full

focus. At the end of the experiment, the people were asked to guess what the picture was. Some of the participants were allowed to see the screen from the beginning (the stage of severe blur) and some from a little later on (when the picture was less blurred). Interestingly, the former group (those who got to see what the latter saw *and more*, since they started watching from an earlier time) got the right answer less frequently. One-quarter of them were right, and of those who started viewing from the less-blurred stage, half got it right. The most plausible explanation has to do with confirmatory bias. Those who started watching from an earlier stage formed opinions based on little information, and then what they saw later merely confirmed the initial opinions.

It is not as if modern theoretical economics teaches us something wrong, for most of these books teach us if-then propositions—if all human beings are rational, if they are subject to the law of diminishing marginal utility, and so on, *then* X, Y, Z will follow, where X could be, for instance, “free trade enhances national income.” Having lived in the world of those “ifs,” all but the clearest minds tend to confuse that world with the real one they inhabit.<sup>17</sup> And the “thens,” which are *parts* of the if-then propositions, become parts of their reality. In some ways it is like a magic show. A good magician in principle shows you everything, but keeps your attention focused on the few things that they want you to see. After a while, what the magician wants you to see becomes your world, and you are ready for illusion.

Much of this book is an attempt to clear the illusions that we have come to acquire through repeated reference to doctrinaire claims, the blinkered observation of the ‘facts’ of economics, and the segueing of textbook models into our beliefs about reality.