
Neosynthesis in Economic Theory*

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ABSTRACT

The large-scale transition from the system of (real) socialism to that of (mixed) capitalism was launched in central and eastern Europe in 1989, followed by the erstwhile republics of the USSR two years later. These developments also served to open the previously closed book of socialist economics to objective study and research. Much has been written on the subject by economists on both sides of the one-time iron curtain. But what are the impressions of an insider looking out? It may come as a surprise that he might view the theoretical foundations of the market economy with serious misgivings.

History knows many civil upheavals, so-called social earthquakes. The world has seen deadly famine, eruptions of violence, the rise and fall of regimes, collapse of monetary systems, waves of bankruptcy, massive unemployment, devastating misery and all kinds of disequilibrium. Today's world is obviously confronted by numerous perils too. At the same time, however, such upheavals serve to stimulate the human mind: old ideas succumb to periodic shocks and this triggers the search for new ideas. Seeing that every radical change is one man's meat and another one's poison, historical turning-points are accompanied with fierce conflicts of ideas. Attack and defence are inseparable companions of progress. In the realm of theory, this means clashes between different schools of thought. However, reconciliation may also take place. Furthermore, what was once

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thought antiquated, may become modern again. All these, and many more, are among the innumerable facets of life.

It is particularly those cases where seemingly incompatible standpoints prove capable of reconciliation after all, that are of interest in the context of the present topic. Depending on one's point of view, (e.g. proprietorial vs. managerial), these are circumstances that give rise to various systemic components that are complementary to one another. The precondition for the neosynthesis in economic theory proposed in this article, has been the disappearance of enmity between the rival economic systems of the world.

Words that signify reconciliation are integration, multiformity, compromise, symbiosis, synthesis and, in particular, system. Words with the opposite connotation include eclecticism, conglomerate, alogism, ideology, scholasticism and any other term that signifies the lack of system. Frequent causes of inaccuracy or error are deliberate distortion motivated by narrow-minded self-interest, the conscious suppression of unwelcome facts, substituting a half-truth for the whole truth, escape from the harshness of real life into an agreeable world of fantasy, in other words, self-deception or surrender to an illusion. It is, of course, not possible to rule out innocent mistakes due to lack of comprehension or deficient information. Moreover, truth, like everything else, has the propensity to run its course and then come to an end.

Consider some examples of ageing and obsolescence. Did Confucius err when he thought that patriarchal succession was tantamount to a divine right? Did Homer err in his belief that wars of plunder were the mainspring of wealth? Did Plato and Aristotle err when they classified working instruments into tools that were dumb, made sounds and could speak? Did Thomas Aquinas err in his conviction that ecclesiastical power was superior to secular power? Did Quesnay err in assuming the landlords to be the foundation on which the whole economy rests? Did Marx err when he ascribed the same function to the proletariat? Did Keynes err when he thought government regulation would prove the salvation of the economy?

One must evidently conclude that all these thinkers expressed the particular circumstances of their time with a great deal of accuracy. It would, however, go against nature to expect that what was considered to be true at a given time in the past, should remain so until the present day. In the field of economics, abiding truths are very rare - if they exist at all. More often than not, misconceptions arise whenever an accepted truth is wrenched from its historical background and judged by present-day standards. By shaping life, time also shapes people and their beliefs. If Keynes had lived today, would he still have taken the same position as

during the 1930s? Hardly so, for every stage of historical development gives birth to new ideas.

Consider now, four theoretically significant episodes in economic history, each one tantamount to a social earthquake. They are (1) the capital accumulation during the last agony of feudalism, (2) the revolutionary wave that rushed through Europe in 1848, (3) the Great Depression and (4) the collapse of sovietism. The first of these triggered a feverish search for order (to avert chaos), the second led to a quest for harmony (to escape revolutionary upheaval), the third - a renewed search for order (to prevent chaos from degenerating into ruin), the fourth - a search for betterment (to avoid a hand-to-mouth existence among the wreckage of the command economy). As always, the alarms and fears produced by these upheavals too, caused ever more innovative ways of thinking to develop.

The search for order in a free market led to the discovery of the "invisible hand". However, not even Adam Smith himself considered this to be a completely reliable or sufficient regulator *per se*, but preferred two-handed to one-handed regulation after all. In point of fact, he associated the role of the so-called visible hand with enforceable contracts, which in turn presupposed the rule of law within a state. At the same time, Smith warned mankind not to overestimate the self-regulating potential of the market. Unfortunately the warning went unheeded, resulting in the harsh social anomalies analysed by Marx later on.

Following the scare of 1848, an infant called microeconomics - also known by the name of marginalism - came into the world in 1870. Seeing that mathematics is a science with an exceptionally harmonious internal structure, it was decided to explore the same source for an equally harmonious model that would fit the economy too. This is humanly understandable. Unfortunately models of this kind are, however, confined to the frictionless world of abstract thought, where they exist in splendid isolation like the gods of antiquity. They cannot smooth over the rough parts of real life. Moreover, in spite of much effort, nobody has ever invented a generally accepted scale for measuring subjective utility. Yet, science is said to begin only there, where objective measurement begins. Therefore, not much more could be expected from microeconomics than its analytical methods based on marginal concepts, since it exemplifies form without content, a so-called empty box.

Marshall, moreover, drew an explicit distinction between function and causation, arguing that economics is a bundle of such complex mutual relations that it may just not be possible to separate cause and effect. Are things really so bad? Descartes, in any case, taught that everything is open to question. The input which enters a system is the direct cause that determines the nature of the output

which emerges from it. Feedback, in contrast, only serves to correct an input without being its primary cause in the process. Systems analysis gives both these relationships a *raison d'être*, at the same time helping us distinguish functionality from causality. General systems theory was still unknown in Marshall's day.

We may note in passing, that the Estonian Encyclopedia, (EE, 1992 : 340) describes microeconomics as an inadequate theory, on account of the dogmatic captivity with which it is associated. Substantially the same verdict is returned by the Finnish economists Pikkarinen¹ and Sutela². They observe that, against expectations, microeconomics is dominated not by positive but by normative reasoning after all, which runs counter to the method of the exact sciences. (The marginal approach implies either a partly canonical, or largely a piously wishful, *modus operandi*.) In the end, there is no dynamic analysis here, despite Marshall's introduction of the time factor. Consequently, microeconomics failed to live up to its historic mission. Its harmonic foundations were undermined by business cycles time and again.

The Great Depression dealt the harmonious marginalist model a staggering blow, showing up the utter vulnerability of the theory in the face of rigorous trials. On both sides of the Atlantic it was realised, more or less simultaneously, that without the aid of the "visible hand" of state intervention, the economy cannot in fact be pulled out of depression. This gave birth to Roosevelt's New Deal programme in America and Keynesian macroeconomic regulation in Europe. Both models reconciled pro- and retroactive intervention, thus laying the foundation of a comprehensive policy. The differences between the American and European models were matters of form rather than content. Both models would, when the time came, prove to have their inevitable historical shortcomings in common too.

In the context of a mixed economy, neoliberalism came to offer some fresh policy options, epitomised by Freedman's monetary model in the United States and the Eucken-Erhard, Ordo-liberal³ model (or the social market economy) in central Europe. As always, these variants also had their strong and weak points. Come what may, the future demands that a model should be adaptable to changing times. Progress never ends: technological innovations give rise to chain reactions that continuously spread their effects to the economy too.

A harsh and in some ways bitter lesson was learned from the fourth social earthquake mentioned above. This once more served to expose the manifest weakness of theory. Neither micro- nor macroeconomics is able to suggest any, at all sensible, solutions to the economies-of-transition⁴ today. Something vital is missing. What can it be? The answer seems to be universality. It is precisely the lack of universality that obstructs the discovery of models powerful enough to fit

untypical situations too. The neoclassical synthesis represented only a very slight movement in the direction of universality. Life today demands a much more far-reaching neosynthesis.

Above all, neosynthesis calls for the renouncement of the artificial and quite unnecessary antagonisms that have taken root in micro-macroeconomics, which are purely ideologically (and therefore unscientifically) motivated. Recall the abovementioned contrast between functionality and causality. We may take Gossen's laws as a case in point. Although Gossen himself expressed them in functional form, they might as well be causally interpreted. On the other hand, there is no reason to contrast Franklin's law of value with the law of demand-and-supply. Firstly, the two laws are easily reconciled and, secondly, it is possible to interpret both of them causally. What has been said here, applies to all known laws in general, whether subjective or objective in kind.

World-wide agreement, as a criterion of truth, has for the present rejected all extreme forms of one-sided regulation as inefficient. Solutions with outcomes that are efficient enough, are as a rule to be found on the so-called combined micro-macro or macro-micro wave bands. Differences are limited to matters of emphasis, depending on whether the "thick end of the stick" that is macroeconomic power happens to be in the hand of the government or the banking sector. A balanced division of power is also conceivable.

In transitional countries, including Estonia, the call for moderation has often been ignored for typically political, selfish or ideological reasons. This is tantamount to gambling. It has meant leaping in the dark, cutting corners or trying to run before one can walk, irrespective of how long one's resources - or luck - may last. The result has been several misadventures. A major disservice to the Estonian economy has been the singularly extremist restitution mania⁵, which provoked the concomitant reaction of deepening apathy. Much self-deception emanated from the simple fact that nobody can turn back the wheel of history.

The state of public responsibility leaves much to be desired. Disjointed legislation paves the way for irresponsible situations. One of my articles in 1992 bore the title "Contract power will save Estonia". Nevertheless, the Republic of Estonia has not yet managed to pass a law of contracts. Someone apparently likes fishing in troubled waters.

Let us, however, return to the subject of neosynthesis. Instead of confrontation and exclusion, we now need to augment economic theory materially, to extend its universality. Whereas great purges in the past have often thrown out the baby with the bathwater, it seems worthwhile starting the quest for renewal precisely among these ejected babies. Recall examples like historicism, causal

analysis, the invariable measure of value, multiplication of services, social economics; to which may be added institutionalism, conflicting objectives, the commodity theory of money, vent for surplus, entrepreneurship and innovation, utopian socialism, and interindustry analysis - the flow of trade that links all sectors of the economy. In contrast, the Smithian approach restricts analysis to the flow of the final product, thus excluding analysis of intermediate product flows.

Say's theory of production gave rise to a series of production function models which, despite subsequent improvements, remained full of holes. Although energy has come to represent an increasingly significant production factor in the world today, this has not been reflected as a major development in its own right. The human contribution, however, is reduced to the same level as those of machines, animals and land. It is impossible to call this a theory in which the human being really plays a central part. Neosynthesis, on the other hand, makes it possible to view all factors, without exception, through a human-centred prism. Moreover, it also allows one to draw a parallel with unified field theory, according to which the universal source of information consists of the trinity: energy, motion and mass. It appears that the economy may be analogously described as

$$Q = f[E(L, K, E')N] \text{ where}$$

Q is the output (quantitative, qualitative) of the economy,

E - contribution of energy sources that serve to release human energy,

L - direct, creative contribution of live human labour,

K - indirect contribution of past labour embodied in capital,

E' - activating, creative contribution of entrepreneurship,

N - passive contribution of land and all natural resources.

Considering the fact that the triad (L, K, E') in a sense amounts to an internally homogeneous term that expresses the triune cause of economic movement, then its analogy with the basic idea of the unified field theory, as the triune source of knowledge, becomes almost complete. The key to neosynthesis is in fact a catholic or pervasive anthropocentrism: in the economy everything begins, and likewise ends, with man. Where man does not go, neither money nor anything else at all related to the economy is to be found. The human being is the Alpha and Omega of economic life.

Against this background, there is reason to assert that the chief impediment to the successful development of economic transition is also a human factor, known as *homo postsovieticus*. This phenomenon is encountered at all tiers of the social edifice, including top government level. A mentality of greed has gained ground in Estonia and stubbornly refuses to retreat before creative thought, without the official codification of economic incentives. But the normalisation thereof is in turn hampered by corrupt self-interest. Hedonistic machinations prevent strategic considerations from gaining ground to a sufficient extent. Incidentally, one-sided and peremptory deregulation is not compatible with general systems theory either, for any complex system is known to fail without the necessary regulation. The present is a time that requires us to take a broader view and to show a better grasp of various acute and painful problems, than micro-macroeconomic theory is capable of providing. The following is the fundamental problem that characterises the transition programmes of the countries embarked on this process: how to achieve the metamorphosis from a fortune-seeking or apathetic *homo postsovieticus* to a soberly calculating and creatively acting *homo oeconomicus*. Thanks precisely to its consistently anthropocentric nature, the theory of neosynthesis may yet, at least to an extent, assist the search for solutions conducive to the discovery of such a turning-point.

ENDNOTES

- ¹ Jukka Pikkarinen, Director, Labour Institute for Economic Research, Helsinki.
- ² Pekka Sutela, Research Officer, Bank of Finland, Helsinki.
- ³ In 1948 the German economist Walter Eucken founded the *Ordo* yearbook, whose title refers to the word and social concept "order".
- ⁴ I.e., economies in transition from the system of (real) socialism to that of (mixed) capitalism.
- ⁵ The official policy since Estonia regained independence in 1991, aimed at restoring to the previous owners or their descendants property confiscated by the Soviet Union after it had annexed the Baltic states in 1940.

REFERENCE

Eesti Entsüklopeedia (EE), vol 6. (1992). Tallinn : Kirjastus "Valgus".