



Faith and Economics

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As I write this article, the nation's unemployment rate has just soared past 10 percent, more than double what it was a year and a half ago. New jobless claims hover at just over a half a million per *week*. While only 45 U.S. banks had failed between January of 2000 and September of 2008, 133 banks failed in the thirteen months that followed. The high priests of the U.S. economy—Federal Reserve chairs, Treasury secretaries, presidents, senators, and representatives—pile more and more sacrifices on the altar in the form of billions of dollars in fiscal stimulus, reductions in interest rates, government purchases of toxic assets, and bank receiverships, all in hopes of placating the dismal spirits responsible for this catastrophe. Yet these offerings appear ineffectual; the economy continues its saturnine course, and we are left to find comfort in the fact that instead of plummeting into the abyss, we seem only to be falling into it.

FAITH AND THE MARKET

This failure of the economy to rebound in response to the Herculean efforts of policy makers is hardly surprising. For all of its strength and complexity, ours is a Tinker Bell economy, whose very vigor depends on our belief in it. Take away that belief—take away our trust in financial institutions and real estate values and job security—and we are left with a sluggish system in which privately held property fails to retain its value. Without faith in the economy, property—be it in the form of houses, or cars, or companies—loses value as demand for it drops. Poten-

Economic faith insists that self-interest motivates people to pursue their own happiness—a reasonable conclusion based on observations from experience. But a Christian understanding of the human—and the human economy—requires acknowledging something about us that moves beyond the old Adam.

tial buyers reduce their participation in the market, both because their own diminished wealth translates to less income for purchases, but also because job insecurity reduces both consumers' willingness to assume and creditors' willingness to offer debt. It is no accident that the word *credit* derives from the Latin *credere*, "to believe." The credit crisis we find ourselves in at present follows directly from our crisis of faith in the economic system. Once we stop believing in this economy, it stops functioning. Until and unless our faith in the economy is restored, we will continue to experience declining housing prices, layoffs, and constrained prospects.

The faith that sustains or threatens free-market economic systems is nothing more sophisticated or more complicated than a belief in momentum as a force affecting social as well as physical phenomena. If housing values are rising, a belief that they should continue to do so attracts others to the housing market, adding the force that propels values ever higher, and rewarding the faith of the investors. But even as momentum explains speculative bubbles, it also explains sell-offs. When confidence in a particular asset, or set of assets, declines due to scandals or new revelations about an asset's true value, investors seek to reduce their holdings, supplying more of the asset to the market. The resulting market glut reinforces the loss of value, and the asset's descent accelerates as other investors dump their holdings. It is little wonder that Roger Babson, the investment advisor largely credited with predicting the 1929 stock market crash, was himself fascinated by Sir Isaac Newton, going so far as to install the parlor from Newton's London home in a building on the Babson College campus, which also boasts a "fourth generation descendant" of the apple tree from Newton's childhood home in Lincolnshire.¹

This faith in market momentum is a form of the "animal faith" described by George Santayana as belief that passes, by "vital constitutional necessity, to belief in discourse, in experience, in substance, in truth and in spirit."² These beliefs reflect "the waxing faith of an animal living in a world which he can observe and sometimes remodel."³ Because of our experience, we believe—*credimus*—that housing will retain its value or lose its value under certain circumstances and, based on this belief, we initiate actions that, in turn, affect the economy in which we live and work. There is nothing ignominious about this and, insofar as economic dicta are based on actual experience, it can be said that they contribute to what Santayana declared the "bold instinctive art...by which man has raised himself to his earthly eminence."⁴ Experience-based knowledge presupposes a "natural world in which it is possible to learn to live better by practicing the arts."⁵

¹R. C. (Rip) Rybnikar, "The Newton Apple Tree," Babson College Archives and Special Collections (updated July 27, 2004), Babson College, 2010, http://www3.babson.edu/Archives/museums_collections/Newton-Apple-Tree.cfm (accessed 8 February 2010).

²George Santayana, *Skepticism and Animal Faith: Introduction to a System of Philosophy* (New York: Charles Scribner's Sons, 1923) 308.

³*Ibid.*, 308–309.

⁴*Ibid.*, 144.

⁵*Ibid.*, 138.

 CLASSICAL ECONOMICS

Economics as a science has its roots in this experience-based knowledge, this animal faith. The protoeconomists—Locke, Mandeville, Smith—made observations of the world based on experience and, from those observations, fashioned a particular view of the world. But like all experience-based knowledge, early economics is limited to the experience of its practitioners, and the positions of these early economists were privileged. Thus John Locke’s observation that enclosing property leads to greater yields than would occur if the same property were managed as a commons is influenced by his experience as physician and advisor to the Earl of Shaftesbury, and is untainted by any firsthand experience with those to whom enclosure brought dislocation and even more extreme poverty. Bernard Mandeville’s observations that “luxury employ[s] a million of the poor and odious pride a million more” are informed by his background as the son of a prominent physician who enjoyed a comfortable life as an educated professional and pamphleteer.⁶ And while his childhood as the son of a widow no doubt exposed young Adam Smith to some hardships, his scholarship to Oxford, his appointment to the faculty at Glasgow University, his employment by the Duke of Buccleuch, and the life pension he was granted by the duke transformed and enriched Smith’s life, materially and intellectually. Smith’s experiences with the landed gentry of his time no doubt helped inform his argument that “if the love of magnificence, a taste for the elegant arts and improvements of human life, for whatever is agreeable in dress, furniture, or equipage...is to be regarded as luxury, sensuality and ostentation...it is certain that luxury, sensuality and ostentation are public benefits.”⁷

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Yet, despite the obvious limitations of experience, the experience-based arguments of the protoeconomists—that economies prosper by promoting the institution of private property while allowing individuals to pursue the self-interested use of this property—are reasonably valid observations. As contemporary economists George Akerlof and Robert Shiller point out, Adam Smith’s theory explains why, even in the height of the Great Depression, 75 percent of the workers who sought jobs were employed. But this experience-based knowledge, grounded as it is in the limited histories of the individuals who have added to it, fails to explain why 25 percent of the U.S. labor force was unemployed in 1933. Classical economic dis-

⁶Bernard Mandeville, *The Fable of the Bees, or Private Vices, Publick Benefits*, vol. 1, ed. F. Kaye (Indianapolis: Liberty Classics, 1988) 24–25 (originally published by Mandeville in 1714).

⁷Adam Smith, *The Theory of Moral Sentiments*, ed. D. Raphael and A. Mafie (Indianapolis: Liberty Classics, 1982) 313 (originally published in 1759).

course predicted that wages would fall in response to rising unemployment, which would, in turn, encourage firms to rehire workers—at a lower wage. Unemployment was seen as a fugacious phenomenon, a market-based problem with a market-based solution. Classical economic discourse could not explain, let alone propose solutions to, the massive unemployment experienced in the Great Depression. The spread of unemployment and poverty throughout the globe provided the shock that, as Santayana describes, “uproots the whole experience. The lights go out on the stage, and discourse loses its momentum.”⁸

THE RISE OF *HOMO ECONOMICUS*

While the economy eventually recovered from the Great Depression, classical economics did not. Experience alone proved both too limited and too complicated to explain a system of exchanges between millions of independent actors engaged in billions of transactions with each other. Beginning with the work of John Maynard Keynes in the 1930s and culminating with the publication of Paul Samuelson’s *Foundation of Economic Analysis* in 1947, economics came to rely increasingly on spartan mathematical formulations of market activity and interpersonal exchanges. But as Asik Radomysler pointed out in 1946, there are fundamental differences between those models, like those employed by Keynes, which are abstractions derived from observations of reality, and those like Samuelson’s, which are based on a convenient or necessary invention, not abstracted from experience, but created as a means to solve a theoretical problem.⁹ The neoclassical school of economic thought employed the latter type of mathematical model and resurrected John Stuart Mill’s economic man, “an arbitrary definition of man, as a being who invariably does that by which he may obtain the greatest amount of necessaries, conveniences, and luxuries, with the smallest quantity of labour and physical self-denial with which they can be obtained in the existing state of knowledge.”¹⁰ While in Mill’s time economic man was the subject of derision and caricature, the same entity, transformed by twentieth-century economists into a mathematical objective function, became the foundation of economic analysis and the prime mover of the economic cosmos.

By simplifying humankind to *homo economicus*, the entire economic system can be portrayed as a series of related objective functions and constraints that has solutions. *Homo economicus* and its single-minded pursuit of the greatest amount of necessaries and conveniences allowed economists like Samuelson “to take incomprehensible verbal debates that go on and on and never end and just *end* them;

⁸Santayana, *Skepticism*, 139.

⁹Asik Radomysler, “Welfare Economics and Economic Policy,” *Economica* 13/51 (1946) 196–198.

¹⁰John Stuart Mill, “Essays on Some Unsettled Questions of Political Economy: On the Definition of Political Economy, and on the Method of Investigation Proper to It,” *London and Westminster Review*, 2nd ed., October 1836 (London: Longmans, Green, Reader & Dyer, 1874) essay 5, paragraph 46. See at the Library of Economics and Liberty Web site (Liberty Fund, Inc., 2003) <http://www.econlib.org/library/Mill/mlUQP5.html#Essay%20V.%20On%20the%20Definition%20of%20Political%20Economy> (accessed 8 February 2010).

formulate the issue in such a way that the question is answerable, and then get the answer.”¹¹ But as is often the case, the expedient solution is not always the best solution. In abandoning rich experience, however biased by position and privilege, for mathematical formalism, economists move dangerously close to solipsism, denying the material world in order to “cast away everything that is not present in their prevalent mood.”¹² The withdrawal of economics from the real world is recognized even by its practitioners. Nobel laureate Ronald Coase once complained that “if economists wished to study the horse, they wouldn’t go and look at horses. They’d sit in their studies and say to themselves, ‘What would I do if I were a horse?’”¹³ Like Santayana’s “secondary mind fed on books,” economists since the Great Depression have been ever more constrained to a universe that is the “after-image” of their learning.¹⁴

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Economic solipsism has several interesting results. First, it has given rise to a delightful collection of economic jokes that are funny because of their characterization of economics as assuming away all the world’s complexity in order to arrive at its stunningly clear and simple solutions. Thus, even as Nobel laureate Sir John Hicks assumed the existence of a diminishing marginal rate of substitution, not because he had observed it in actuality, but because without it, economic equilibria will not be stable,¹⁵ so one joke that every initiate to economics hears as a graduate student describes how an economist, stuck on a desert island with a physicist and a chemist, rejects his companions’ practical solutions to the problem of how to open the can of soup that has washed ashore with the simple solution, “Let’s assume that we have a can opener.” A collection of economic lightbulb jokes—and there are many—pokes fun at the striking tendency of these economic problems cast as mathematical models to find that the best possible solution to any economic problem is that which arises from doing nothing and letting the market take care of things. Thus the response to “How many economists does it take to change a lightbulb?” is invariably some variation on, “None. If the lightbulb needed changing, the market would have already done it.”

¹¹Robert Lucas, as quoted in Arjo Klammer, *Conversations with Economists* (Totowa, NJ: Rowman and Allenheld, 1983) 49.

¹²Santayana, *Skepticism*, 18–19.

¹³Ronald Coase, “The Task of the Society” (opening address, Annual Conference, International Society of New Institutional Economics, Washington, DC, September 17, 1999). See at the Ronald Coase Institute Web site (The Ronald Coase Institute, 2000–2010), <http://www.coase.org/coasespeech.htm> (accessed 8 February 2010).

¹⁴Santayana, *Skepticism*, 19.

¹⁵Sir John Hicks, *Value and Capital: An Inquiry into Some Fundamental Principles of Economic Theory* (Oxford: Clarendon Press, 1939) 21; quoted in A. Radomysler, “Welfare Economics and Economic Policy,” *Economica* 13/51 (August 1946) 195.

But aside from being a fount of humor—no other social science has its own joke pages on the Web—by limiting the world to just that which exists within its mathematical models, economic solipsism is able to arrive at and defend the Panglossian conclusion that markets alone deliver the best of all possible worlds. And to the extent that the world of economics is populated solely by *homo economici*, the conclusion is reasonably valid. So long as all of us, rich and poor alike, mimic Mill's economic man and care only to "obtain the greatest amount of necessities, conveniences, and luxuries, with the smallest quantity of labour and physical self-denial," and so long as necessities, conveniences, and luxuries all exchange in markets, then markets will deliver the goods, and deliver more of them than other systems. But even this success is not unqualified: while market economies will generally produce more goods and services than other economies, not everyone within a market economy will necessarily enjoy more goods and services than he or she would under other production and distribution systems. How one fares in a market economy depends in large part on one's initial endowment. In a market system in which privately owned goods and services are voluntarily exchanged, individuals with paltry endowments face constrained prospects.

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In the world that exists inside of the economic mind, individual *homo economici* make labor, investment, consumption, and savings decisions according to which choices promise to maximize individual happiness, or utility, over their lifetimes. These choices are constrained only by the individuals' initial endowments. Most importantly, choices are not constrained by familial obligations, cultural constraints, and taboos, nor repressive nor unstable governments. Happiness accumulates to the individual on the basis of his or her ability to acquire income, wealth, and utility-generating consumption bundles. Happiness is not a function of love or hope, of wholeness or peace. Insofar as *homo economici* behave altruistically, it is because altruistic behavior makes them feel happier. Every choice *homo economici* engage in—whether between tea and coffee, charity and penuriousness, acceptance or rejection of God—is decided by a simple determination of which choice will likely generate the greatest utility.

It is easy to see how freedom becomes the only moral imperative in this world, and how the Panglossian conclusion follows from this set of behavioral assumptions. When options are constrained, when certain goods are not allowed to be sold, when certain jobs are prohibited, or when government taxes away wealth or income, *homo economici* are thwarted in their attempts to attain maximum utility. Only if we allow *homo economicus* the freedom to choose among all his or her

various options can we be assured that our economic person will be able to attain the maximum level of happiness. If all *homo economici* are allowed the freedom to pursue their choices, and each individual free to attain his or her maximum possible utility, the total utility enjoyed by society, the social welfare, is itself maximized. It is the best of all possible worlds.

LIMITATIONS OF *HOMO ECONOMICUS*

Given freedom of choice, it follows that whatever sweatshops *homo economici* work in, whatever malnutrition or illness they or their children experience, whatever bridges they sleep under, represent the best possible working situations, the best possible health outcomes, and the best possible shelter for these creatures. Thus, we are told by those whose faith is in the market that sweatshops are “a good deal for the people who work in them,” as sweatshop labor represents “the best of a bunch of bad choices.”¹⁶ Improving on the set of choices available to sweatshop workers would require intervention in the market, and that would mean adding a constraint to someone’s behavior, reducing the set of choices available to some members of this society and, thereby, reducing the level of social welfare. However, even if constraints reduce overall social welfare, it is entirely possible that introducing a set of constraints on the exploitation of laborers might raise the welfare of that class of laborers. The relevant question that economics poses for us when considering the desirability of sweatshops is whether our attempts to help the least among us make them better or worse off.

And this raises two questions that we need to ask ourselves as we consider our response to and responsibilities within a market system. First, if we wish to assess the impact of economic policies on the least of us, we must consider the extent to which economic values translate into legitimate measures of social welfare. And second, we must inquire as to the extent we are justified in relying on the policy prescriptions emanating from neoclassical economic models as a means of fulfilling a Christian calling to be stewards of creation and lovers of our neighbors.

Several characteristics of both the composition and the value of the goods and services produced in a market economy detract from their unconditional adoption as measures of social welfare. First, as goods are supplied in a market economy in response to consumers’ willingness and *ability* to pay for them, it follows that those goods valued by those who possess the means to pay for them are more likely to be supplied than those goods that meet the needs of fellow consumers, fellow members of society, lacking the ability to pay. This explains in part how both homelessness and the average size of new homes have increased with increases in income inequality here in the United States. Second, market economies respond to consumer desires, however poorly informed these might be. A market economy can as

¹⁶Hoover Institution Office of Public Affairs, “The Case for Sweatshops,” *Hoover Daily Report*, February 7, 2000. See at Hoover Institution Web site (Board of Trustees of Leland Stanford Junior University, 2010), <http://www.hoover.org/pubaffairs/dailyreport/archive/2864991.html>. (accessed 8 February 2010).

easily produce housing and food and education as it can produce snake oil and Pet Rocks and methamphetamine. Measuring social welfare by the quantity and the value of the goods produced by an economy presupposes that housing contributes no more, dollar-for-dollar, to social welfare than Pet Rocks, or that food is dollar-for-dollar equally efficacious in promoting social welfare as is meth. To the extent that an economy produces wasteful luxury or harmful toxins, measures of economic activity such as the gross domestic product (GDP) are poor indicators of social welfare.

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Not only do measures of social welfare as denominated in the coin of the market system fail to provide accurate measures of social welfare, but they also fail to reflect the impact of the pursuit of maximum economic welfare on the least among us. The empirical link between economic growth and improved welfare among the least of us is not as strong as the strength of the rhetorical argument that links rising tides with the lifting of all boats. Indeed, international estimates of the impact of growth in national GDP on the percent of a nation's population living on less than a dollar a day suggest that the boats of the poor do not rise with the rest of those in the regatta. Rather, averaged across all economies, a 1 percent increase in per capita GDP appears to result in only a 0.7 percent reduction in the number of people living in extreme poverty.¹⁷ Furthermore, evidence exists that the number of desperately poor might actually increase with rising GDP if increases in GDP contribute to increases in income inequality. Empirical research by Patrick Honohan at the World Bank reveals that as the proportion of income going to the wealthiest 10 percent of a nation's population increases by one percentage point, the population of individuals living on less than a dollar a day increases by one-half of a percentage point.¹⁸ Rising tides might actually sink some boats.

CHRISTIANS AND ECONOMIC FAITH

As Christians attempt to discern their callings, they need to be wary of an economic faith that argues the paradoxical conclusion that self-interested actions, undisciplined by charity, by love, or by calling, guide all as if by an invisible hand to the best possible outcome. If Christians could truly love their neighbors by passive participation in a free-market system, there would be no need for Christ to have commanded them to extend love to their neighbors. Christ does not command his followers to feed or clothe themselves; they do this without his edict. But he does call on his followers to feed his sheep and clothe the naked; their own self-

¹⁷Timothy Besley and Robin Burgess, "Halving Global Poverty," *The Journal of Economic Perspectives* 17/3 (Summer 2003) 3–22.

¹⁸Patrick Honohan, "Inequality and Poverty," *The Journal of Economic Perspectives* 18/2 (Spring 2004) 271–272.

interested behavior would not immediately lead to the care of others. If Christians could truly love their neighbors by pursuing self-interest, Christ's call to deny themselves and follow him makes no sense.

Economic faith is nothing other than belief that self-interest motivates people to pursue their own happiness. To the extent that this faith is based on observations from experience, it is a useful tool for predicting human responses to external stimuli and novel situations. But to the extent that economics focuses its observations on the actions of a fallen, self-interested humanity, economic faith is simply a belief that studying the energies and motivations of old Adam will help us understand our world, and that some good will come from that understanding. And while economists are content to accept old Adam as a part of human nature and use him as a basis to understand the world around us, Christians celebrate Adam's daily death in the waters of baptism. As such, while old Adam might be a useful reference point for understanding the economy, he hardly provides us with the compass we need to plot its direction, nor the balance we need to weigh its diverse options. ⊕

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