

Chapter 2

A Word on Economics

Economists are not some innocent technicians who did a decent job within the narrow confines of their expertise until they were collectively wrong-footed by a once-in-a-century disaster that no one could have predicted... Economics as it has been practised in the last three decades has been positively harmful for most people.

British political philosopher, author and former School Professor of European Thought at the London School of Economics John Gray (2010) reviewing Ha-Joon Chang's book, 23 *Things They Don't Tell You About Capitalism*.

Capitalism is best conceived and practised, runs the theory, by hunter-gatherer bankers and entrepreneurs owing no allegiance to the state or society. This is nonsense. Business and the state co-generate wealth in a system of complex mutual dependence. Markets are beset by mood swings and uncertainty which, if not offset by government action, lead to violent oscillations. Capitalism without responsibility or proportionality degrades into racketeering and exploitation.

Will Hutton (2011). The ailing euro is part of a wider crisis. Our capitalist system is near meltdown. *The Observer* 18 September.

2.1 Economics and Education Reform

There seem to be two worlds in which education reform, along with everything else, proceeds. In one a purely statistical and theoretical view of economics prevails. In the other sociology, a view informed by studies of the social interaction of people. To move from the former view to the latter is to enter through a kind of 'green door' from a society dominated by individual utility maximisation to one more concerned with social value, one which recognises the sometimes irrational behaviour of people. One is based entirely in theory and has a utility related to its alleged predictability derived from sophisticated mathematics, a predictability which in most cases is at best difficult to test. The other is supported by extensive

research on what people value and what they do not and how they actually behave and how that is influenced by their stated values.

This essay reviews the various approaches to economics and especially considers the nature of neoclassical economics and its consequences, ultimately for the advance of society at large and particularly education. I review the basic approaches of neoclassical economics and then the evidence for its failures and inadequacies. I believe it is clear that not only has neoclassical economics led to substantial inequities and disruptions in society but driven education reforms in a wholly negative direction largely favouring the more privileged in society. In the final analysis, neoclassical economics does not appropriately describe human society and human behaviour. That is a view in fact held by many prominent economists and supported by research.

If any reader thinks this essay is too harsh or not relevant, they might take the time to watch at least the trailers of the films, *The Inside Job*, *Company Men* and *The Corporation*. There are many comments on economics and the world of commerce far harsher than anything I say in this essay. It has been observed, for instance by Madeleine Bunting in *The Guardian* of 30 May 2011 that *Inside Job* does for banking what *An Inconvenient Truth* did for climate change.

Economics as a discipline is not to be uniformly distrusted: much of it is based on well analysed empirical data, even over the long run. Much of it is intellectually challenging. But the economics which dominates society in most western countries is not like that and the popular economic commentary which dominates much of the media, especially the daily diet of ‘analysis’ of movements, actual or predicted, of various indicators and issues such as government budgets, is often worse! The carefully reasoned analysis found in print media such as the *New York Review of Books* and the business pages of some of the broadsheets seldom gets to the front page and certainly seldom reaches the minds of politicians or some so-called think tanks whose conclusions are overwhelmed by their preconceived ideologies.

2.2 The Basics of Neoclassical Economics

Whilst economics is in reality a mixture of sociology and statistics, the prevailing view over the last 40 or so years has largely ignored sociology and the statistics have become sophisticated, even arcane. Moreover what is readily analysed and for which there is substantial data is the focus whilst the more difficult and the rare event is put aside. Humans are viewed as rational utility maximisers motivated principally by financial incentives, competition is considered to drive people and therefore organisations towards efficiency and therefore lower prices for goods and services.

The market is self regulating and ultimately acts as a clearing house reconciling conflicts, economic growth is the path to society’s greater wealth and the solution to problems such as the need for more jobs. Deleterious consequences, such as increasing inequality, are seldom considered. Government intervention is

eschewed. Neoclassical economics has driven the agenda of public policy, usually referred to as neoliberalism, for several decades.

As a matter of course, costs of transactions which cannot be directly charged, particularly those which would seem to apply generally such as public goods like water and forests, are considered to be externalities and are not counted in the pricing. Pollution produced by coal fired power stations is not included in calculating the cost to the energy generator, and therefore is not charged to the consumer: consequently the cost has to be met at a later time, usually by the government, in other words the public.

Where the resource is not replaceable there is no brake on its consumption. This situation is captured by the well known phrase, ‘capitalise the gains and socialise the losses’: the transfer of billions of dollars from governments to banks to stave off likely financial collapse following the GFC is an example. Many of these activities receive government subsidy whilst at the same time those who benefit declaim against subsidies for other activities. The result is a distortion of choice. Heavily subsidised sport is often compared with less well subsidised arts activities, a frequently expressed view being that the arts should pay for themselves.

Consumption is favoured as the engine of growth and a larger population is needed to help achieve that. Innovative technology is believed to arise to solve any problems which might emerge. Individuals are favoured over communities. Individuals are considered responsible for their future welfare other than in exceptional circumstances. That growth in consumption cannot continue indefinitely seems not apparent to those economists whose opinions are quoted every day in the media as various statistics are reeled off to a seemingly ignorant population.

Professor John Quiggin of the University of Queensland has summarised five significant ideas central to neoclassical economics which have little or no basis in fact but continue to be treated as valid (Quiggin 2010):

- the notion that the period beginning in 1985 was one of unparalleled macro-economic stability which has been comprehensively refuted by the GFC,
- the efficient market hypothesis which asserts that the prices generated by financial markets represent the best possible estimate of the value of any investment which has been shown to be absurd by events such as the dot-com bubble, macroeconomic analysis should not be concerned with observable realities such as booms and busts but with theoretical consequences of optimizing behaviour by rational actors—branded by Paul Krugman as mistaking beauty for truth,
- the trickle down hypothesis which supposes that policies benefitting the wealthy will eventually help everyone which was conclusively refuted by postwar experience and the extraordinarily limited economic mobility in countries like the USA (and the experience of the last several decades in which inequities in wealth have increased enormously),
- privatisation, the notion that nearly any function undertaken by government would be done more effectively and efficiently by the private sector which has simply replaced public monopoly with private monopoly whilst numerous commercial entities have had to seek government bailouts.

2.3 Individuals and Choice: Limits to Government

The theoretical base of neoclassical economics derives from the writings of a number of economists, especially at the University of Chicago, who had arrived there from Europe, most particularly Austria, in the years after the close of the First World War (Judt 2009). They had experienced the failure of a centralised economy: therefore a different economic model was needed. Notable among them were Friedrich Hayek and Joseph Schumpeter. Milton Friedman of the University of Chicago became the principal promoter of neoclassical economics after the Second World War and received the Nobel Prize for his efforts. These views found fertile ground in a country with an ideology grounded in individual freedom and choice and a belief that commerce must be free from government ‘interference’.

Social democracy, its advocacy for intervention by government at appropriate times, such as when benefits to the community would not otherwise be provided and its concern for the community at large including those less fortunate, as advocated by the English economist John Maynard Keynes, was left behind in the latter day striving for individual gain.

Private enterprise in the context of neoliberal philosophy is considered inherently able to perform more efficiently than government. Government is believed to be a brake on, to crowd out, the free operation of business and the market which itself is (asserted to be) self regulating. Indeed business, including the media, is said to be self-regulating, even in the face of appalling invasions of privacy through hacking of personal phones, not to mention frequent failures to report issues bearing on important matters because of political positions adopted by particular media. Attempts by government to even consider regulation are attacked as unnecessary intrusions into the market and as attacks on free speech. When numerous financial institutions grossly overreached themselves governments rushed to bail them out: the ordinary citizens who suffered through loss of their houses as a result of foreclosures and so on were largely ignored, left to fend for themselves.

The first responsibility of business enterprises is now considered to be the generation of wealth for shareholders, not the provision of goods or services to customers at an optimal quality and price, which once was seen as the purpose. A tension is asserted to exist between the motivation of executives on the one hand and the shareholders. Boards, representing the shareholders, therefore need performance targets to assist oversight and ensure transparency and accountability.

Managerialism—management in every enterprise is a management function—has become dominant in government over the last 30 years supported by business lobby groups. Senior executives are appointed on fixed terms and enrolled in merit pay schemes. Investment in training and development is poor; all but core functions are outsourced. Public–private partnerships for infrastructure projects are favoured though they ended up costing more than they would have if they were managed within government, partly because of unfavourable interest rates on debt. Guarantees to pay the commercial partner in the event of loss and excessively

optimistic financial estimates mean increasing government debt (Walker and Walker 2008). Substantial downsizing led to significant loss of corporate memory and inability to manage complex contracts. Financial matters and corporate functions have achieved greater prominence.

All of this has led, in some countries, to an undermining of democratic government through the marginalisation of parliament and parliamentary accountability by the head of government and senior ministers and advisors (Foster 2005). UK Prime Minister Tony Blair replaced cabinet by 'prime ministerial government', Australian Prime Minister Kevin Rudd was notable for the way he and three other Ministers controlled all cabinet decisions (Marr 2010).

Above all effectiveness has been conflated with efficiency, microeconomic reform such as holding wages down, reducing extra allowances for overtime and so on, has led to decline in commitment to the enterprise and therefore a decline in productivity (Gittins 2011a). Despite this these strategies continue and so does the drive to reduce employee benefits. No reference was made to the substantial evidence about these matters when the Business Council of Australia and others praised the decision of Fair Work Australia to allow employees to trade off their holidays and other benefits for higher wages.

In Australia, Prime Minister Gillard agreed February 2012 to establish a Business Advisory Forum, 'to advise governments on how best to coordinate and progress the remaining areas of competition and regulatory reform; and to nominate new areas of regulatory reform that will help lift productivity and drive investment' (Anon 2012).

By way of contrast, in many European countries governments still provide high levels of social welfare without negative consequences for the economy and productivity levels. Interestingly, French people spend more time eating and more time sleeping than the average for people in OECD countries and have amongst the very highest life expectancy. As widely reported, in the 2010–2011 global competitiveness ranking compiled by the World Economic Forum France was ranked 15th, having risen 15 places in 5 years, ahead of Australia (which had fallen 5 places in 5 years); the US was fourth after Switzerland, Sweden and Singapore. By 2012 Switzerland was first followed by Singapore and Finland, then Sweden; the US was 7th and Australia 20th ahead of France.

Importantly there is increasing interest in constructing an index representing many different aspects of life to sit alongside such strictly economic indicators as Gross National Product or GDP which measures only economic performance and that somewhat unreliably. Compilation of an index of social progress for Australia has recently started; the OECD began publishing its 'better life index' in 2011 (Gittins 2011b). Yet neoclassical economics consistently emphasises choices relating to material goals and links pursuit of such goals to happiness. Much of the striving for material goods amounts to no more than a seeking of positional goods, things which relate only to attaining status in the eyes of others. Things are acquired to impress others whom one doesn't know very well and who actually don't care anyway.

2.4 Privatisation of Government Services

The consequences of these changes have been disastrous in some cases and led to declines in quality of service in most cases!

In Bolivia the World Bank made water privatization a condition of a loan to the government. The public water system was privatized in 1997, sold to a water company owned by a consortium led by the French water giant Suez, the World Bank and others. (A report in 2005 on water privatisation in Latin America by Puerto Rican journalist Carmelo Ruiz Marrero is featured on numerous websites.). Nine years later the Bolivian government cancelled the contract with Aguas del Illimani following several days of public protests in El Alto, a satellite city of La Paz, at overcharging of customers and failure to invest enough to expand water services to poor neighbourhoods; costs to connect to the system exceeded more than half a year's income at the Bolivian minimum wage. Similar outcomes have occurred in other countries.

The clever salesmanship and development of sophisticated mathematically-based financial instruments sold in complicated ways to other enterprises and eventually to investors who ended up losing their money and their property is a typical outcome of the GFC. In Jefferson County in Alabama USA, the county seat of which is the city of Birmingham, a sewage system project originally estimated to cost around \$250 millions ended up costing several billions after complicated interest rate swaps were arranged by corrupt country officials and bank officers. County employees lost their jobs, a number of people were paid ongoing bribes, the banks ended up being fined, sewage rates were increased; at the end the county was left with a debt equal to more than \$4,000 per resident. In November 2011 leaders of the Jefferson County voted to file for a \$4.1bn bankruptcy, the costliest US municipal failure ever (Anon 2011).

The notion that in general, the private sector performs more efficiently than government is an exaggeration and in some cases, wrong! A comprehensive study by Christopher Stone at the Centre for Policy Development in Australia shows that in terms of technical efficiency, doing the same job more cheaply, the stripping out of expertise in government agencies in order to contract out the work led to projects costing more than when technical expertise was retained (Stone 2013a, b). Analysing the much criticised 'Building the Education Revolution' or BER, wrongly characterised by some as wasting a lot of money, costed significantly more in New South Wales and Victoria which had to rely entirely on external contractors than in Queensland which has maintained a relatively strong public works skills capacity.

Private schools, private hospitals and private health insurance, for instance, are not more efficient than single public systems. Public-private partnerships are more expensive and the private sector certainly does not address 'dynamic efficiency', such as investing in high speed rail. Unfortunately in Australia, risk-averse governments won't either, continuing to build roads when clearly public transport would achieve much greater efficiency with less cost to the environment. And

certainly regulations and work practices are not better enforced in the private sector, quite the reverse.

Stone concludes, 'Our public sector suffers the plight of the anorexic. No matter how thin it gets there are voices saying it's too fat. Do we really want a size zero government? The word 'efficiency' is often misused to mean 'cuts', and some cuts to public services can end up costing us much more than they save. When it comes to privatisation or outsourcing, too many of our politicians have tunnel vision. They can only see the private sector as efficient and are blind when it fails...' The benefits and disadvantages of outsourcing and privatisation need to be carefully considered instead of adopting endless cuts to the public sector through 'a blind faith in market solutions'

2.5 The Global Financial Crisis and Its Consequences

The GFC has significantly increased unemployment in many countries including the US and Europe. That has been further exacerbated by the response of governments to the huge debt incurred through their bail out of banks and other actions. Many banks in those countries had loaned excessive amounts of money for purchase of housing, often without proper consideration of the ability of borrowers to repay the loans. When housing prices crashed as a result of bank's risky lending, many borrowers found their debt greatly exceeding the revised value of their housing. In many cases they remained liable for the debt even when their home was resumed by the lender.

Revisions of legislation which might limit the recurrence of further actions of the kind which led to the GFC met with strong opposition from the financial industry. However, financial institutions resumed their payment of large bonuses to executives not long after governments bailed them out.

A legion of economic writers, Nobel Prize winning economists and others, have filled the pages of scholarly journals, newspapers, magazines and the radio air-waves and television screens with commentary pointing to the failure of the financial system and its economic base. Paul Krugman, Professor of Economics at Princeton University, 2008 Nobel Prizewinner and *New York Times* columnist, observes, 'the economics profession went astray because economists, as a group, mistook beauty, clad in impressive-looking mathematics, for truth. Until the Great Depression, most economists clung to a vision of capitalism as a perfect or nearly perfect system. That vision wasn't sustainable in the face of mass unemployment, but as memories of the Depression faded, economists fell back in love with the old, idealized vision of an economy in which rational individuals interact in perfect markets, this time gussied up with fancy equations.' (Krugman 2009).

Influential lobbyists work hard to convince governments that they themselves should reduce expenditures and deficits, that excessive control of financial institutions would produce serious distortions and economic hardship. Professor Andrew Kakabadse, Professor of International Management Development at

Cranfield University School of Management in the UK and author of the book *The Elephant Hunters* (Lake, Kakabadse and Kakabadse 2008) about the GFC, told Phillip Adams, presenter of the ABC RN program *Late Night Live* in October 2008 that senior managers reporting their concerns about the future consequences of sophisticated financial instruments such as credit default swaps and the like can be informed by their executives and boards that their concern is misplaced and not conducive to further employment.

Staff of financial entities and officials at the highest levels, as well as academic economists, have failed to consider the possibilities of unlikely events. A week of intense discussions amongst leading academic economists at a workshop on modelling financial markets in 2008 (Collander 2008) concluded, 'The economics profession appears to have been unaware of the long build-up to the current worldwide financial crisis and to have significantly underestimated its dimensions once it started to unfold. In our view, this lack of understanding is due to a misallocation of research efforts in economics... The economics profession has failed in communicating the limitations, weaknesses, and even dangers of its preferred models to the public.'

Those conclusions closely resemble the views of Nassim Taleb, essayist, mathematical trader and author of *The Black Swan*. Taleb's central belief is scepticism about the predictability of markets and people's biases in the attribution of skills, how we are fooled by randomness (Taleb 2004). 'Much of what happens in history', he notes, 'comes from Black Swan dynamics, very large, sudden, and totally unpredictable outliers, while much of what we usually talk about is almost pure noise. Our track record in predicting those events is dismal; yet by some mechanism called the hindsight bias we think that we understand them. We have a bad habit of finding 'laws' in history (by fitting stories to events and detecting false patterns); we are drivers looking through the rear view mirror while convinced we are looking ahead.' Taleb advances these ideas in his latest book, *Antifragile*. (See Sect. 11.2)

In February 2008, the President of the French Republic, Nicholas Sarkozy, unsatisfied with the present state of statistical information about the economy and the society, asked three leading economists, Joseph Stiglitz, Amartya Sen and Jean Paul Fitoussi to create an investigative Commission, subsequently called 'The Commission on the Measurement of Economic Performance and Social Progress' (Stiglitz, Sen and Fitoussi 2009).

The Commission concluded that the low level of public trust in official figures has a clear impact on the way in which public discourse about the conditions of the economy and necessary policies takes place.

Three years on from the depths of the GFC, problems remained which had not been born by financial institutions. Madeleine Bunting (2011) writing in *The Guardian* newspaper proclaims that 'outrage against the banks is no longer a leftwing hobby as the fact that the greed and irresponsibility of some in the financial community were the cause'. Bunting observes '... finance has intertwined itself intimately into the political process in both the US and the UK.' In many cases banks are failing to meet their targets of lending agreed with governments who bailed them out.

Lobbying has ensured some crucial reform initiatives hit the buffers (Taibbi 2011b). Senior executives in the Securities and Exchange Commission in the US authorized systematic destruction of the records of preliminary investigations of possible crimes by financial institutions, where decisions had been made not to proceed further. Those executives are frequently appointed to senior positions in the companies which the SEC had been investigating.

In November 2011 Nobel prizewinner and Columbia University professor Joseph Stiglitz, noted economic analyst Nouriel Roubini and biographer of Keynes Robert Skidelsky, writing on the Project Syndicate website, all strongly criticised the increasing inequality brought about by the exercise of political influence and the anti-competitive practices of financial institutions (Stiglitz), strongly urged easing of monetary policy by the European Central Bank to reflate the Eurozone periphery and criticised fiscal austerity (Roubini) and urged that a growth strategy be adopted by the Europeans (Skidelsky). All criticized the refusal of the German Government and the European Central Bank to take a more interventionist role. Paul Krugman, in numerous articles in the *New York Times*, has consistently urged similar approaches.

The austerity budgets adopted by peripheral economies of the European Union have meant shrinkage of the economy: yet an expansion of the private sector was anticipated by some economists as justifying the austerity! That in turn has meant a decline in jobs—employment prospects in the UK have been described as the worst for almost a year (Allen 2011): large numbers of skilled young professionals are leaving for South America and Australia. Quite how the decline in the professional workforce will assist economic growth in later years remains a puzzle to put it mildly. As well, poorer people are in some cases abandoning their very young children, no longer able to care for them (Hadjimatheou 2012). In the US survival through the economic downturn for some pensioners has meant selling their pensions for a lump-sum payment. Repayment of debt is treated as a moral issue. One of the alternative ways in which a country's debt could be dealt with is to institute a scheme comparable with the US system of Chapter 11 bankruptcy which would allow writing off of old debt and borrowing to finance new growth (Kuttner 2013).

And when glaring errors are found in the methods and forecasts made by economists, workarounds are found and nothing much changes. JP Morgan's "London Whale" venture went bad because modellers divided by a sum instead of an average; the calculations leading to the view that once government debt reached 90 % of gross domestic product economic growth dropped off was shown to be due to an Excel spreadsheet error (Krugman 2013a, b) which was uncovered by an economics student! These revelations had little effect. In the case of the miscalculation of the impact of government debt, the economists involved, Carmen Reinhart and Kenneth Rogoff of Harvard, faced criticism from the start, yet have continued to promote their views. But as Paul Krugman observed, another dubious piece of economic analysis will be found to be canonised by the 'usual suspects' and the depression will go on. 'Policy makers abandoned the unemployed and turned to austerity because they wanted to, not because they had to.' The proposition that governments should not spend more than they gain in revenue is

astonishingly pervasive: the view is that countries that run up large debt, such as Greece, Spain, Portugal and Ireland, have to be punished. The consequences have been disastrous.

The head of the International Monetary Fund (IMF), Christine Lagarde, expressed great concern at the policies of the UK government but it made little difference. Chancellor George Osborne was told to invest more in social housing, schools and road repairs (Elliott 2013). Early in 2013 the IMF revealed that whereas they had previously asserted that for every dollar governments reduced their budgets, economic growth would be reduced by half that, in fact the impact was three times greater, \$1.50 instead of 50c. Did European countries halt their austerity measures which have driven millions into unemployment? No. These developments were not recalled either when the Grattan Institute in Australia in late April 2013 forecast years of government debt at all levels; other analysts rushed to agree. Commentators spoke in authoritative voices pointing out that belts would have to be tightened: Australians had come to expect too much from governments! The relatively tiny level of government debt and the relatively small budget deficits were ignored. It was all reduced to the frame of our household!

Equities markets are supposed to be responsive to economic trends and be self regulating. Four years after the research was first announced, statements are appearing that ‘the world could be heading for a major economic crisis as stock markets inflate an investment bubble in fossil fuels to the tune of trillions of dollars’ (Carrington 2013). A report by Nicholas, Lord Stern of the UK pointed out that almost all investors and regulators were failing to take note of the research by scientists at Potsdam Institute for Climate Impact Research in Germany, published in 2009 (Meinshausen et al. 2009; Eickemeier 2009), which concluded less than a quarter of the proven fossil fuel reserves can be burnt and emitted between now and 2050, if global warming is to be limited to two degrees Celsius (2 °C).

A report, *Unburnable Carbon* 2013, prepared by the Carbon Tracker Initiative and the London School of Economics’ Grantham Research Institute (Hutton 2013) showed that stock markets worldwide are cumulatively valuing coal, oil and energy companies’ huge reserves of fossil fuels as if they will all be burned and every year spending billions of dollars on finding new reserves. In other words, there is either a carbon bubble with investors and companies wildly over-speculating on the value of owning fuel reserves that can never be burned, or nobody believes there is the remotest chance that the world will stick to the limits on fossil fuel use congruent with containing global warming.

Novelist and writer on ethnography, history, and social theory Richard Sennett points to the way these countries deal with this unemployment: leave it to voluntary associations (Sennett 2011). He points out that different solutions are found along Europe’s northern rim—in Scandinavia, Germany and the Netherlands. There governments have protected established companies, especially small companies, providing capital for growth when banks won’t lend it. Norway and Sweden have made concerted efforts to include young people in starter jobs; youth unemployment stands at about 8 %. Germans put big resources into youth training schemes; the Dutch effectively supplement the wages of part-time employees.

Factories in these countries have long explored how to deal humanely with automation, and tried in many different ways to counteract the outsourcing of jobs.

A survey of 11,000 people in 23 countries in late 2011 found unemployment to be the world's fastest-rising worry (Gregory 2011). Welfare changes imposed by the UK government have impacted those least able to afford them. Of the jobs lost in the aftermath of the GFC a disproportionate number have been one's in construction, manufacturing and high finance, jobs traditionally occupied by men (Rosin 2012). The lessons of President F.D. Roosevelt in overcoming the Great Depression of the 1930s in the US have been ignored (Bennett and Walker 2011).

2.6 An Alternative View: Lessons from Behavioural Economics

Studies by Daniel Kahneman, winner of the Nobel Prize in Economics in 2002, and Amos Tversky, contradict the claim that the freest market produces the best economic outcome but rather than being the rational individual, maximizing utility in an institutional vacuum imagined by the market model they are real people (Kuttner 1997). 'People will typically charge more to give something up than to acquire the identical article... People help strangers, return wallets, leave generous tips in restaurants they will never visit again, give donations to public radio when theory would predict they would rationally "free-ride", and engage in other acts that suggest they value general norms of fairness. To conceive of altruism as a special form of selfishness misses the point utterly.'

Economist George Akerlof, Professor at the University of California Berkeley, shared the 2001 Nobel Prize for Economics with Joseph Stiglitz. In a celebrated address in 2007 he pointed out that the omission of people's normative behaviour from economists' models results in quite important deviations of predictions from behaviour which is actually observed: positive economics privileges models without norms... He concludes 'Economic decisions may not be as duplicable as biological processes, but the basic reason why science intensively studies the microscopic applies to economics as well. The individual economic unit, be it a firm, a consumer, or an employee, behaves the way it does *for a reason*. And if these actors behave as they do for a reason, we can expect to find those reasons from the structures that we see in close observation; and because of those structures their behavior will also tend to be duplicated.' (Akerlof 2007)

Studies of behavioural economics have attracted increasing attention (Cassidy 2008, McAuley 2010). They show that people tend to be subject to mental quirks and biases including inertia, overconfidence and loss aversion.

Levels of cooperative behaviour and reciprocity, perception of and tolerance for inequalities in society differ amongst people, especially between Asian societies and western societies. Whilst intrinsic self esteem as expressed by association of self with positive events and feelings may not differ, extrinsic self-esteem

expressed as preparedness to admit positive feelings about one's self differ substantially, being low in east Asian societies and high in western societies (Mitchell 2010). Statistics compiled by the OECD (2011) and by Gert Hoffstede, Dutch pioneer in his research of cross-cultural groups and organizations, available on his website, elucidate these points.

Tim Jackson, Professor of Sustainability at the University of Surrey, pointed out in his Deakin Lecture in Melbourne in 2010 (Jackson 2010) 'Prosperity without Growth' that the concept of prosperity as an ongoing drive for growth is inconsistent with human nature. He observed that in fact prosperity is not about income growth but about health of family, trust of friends, security of one's community, participation in the life of society '... just asking people in the street tells you that prosperity... is about some sense perhaps of having a meaningful life and a hope for the future... 'there is no evidence in social psychology that we really are the narrow, materialistic, selfish, individualistic consumers that the economy would have us believe that we are. Social psychology talks much more about tensions between selfishness and other regarding behaviour. It talks about tensions between novelty seeking and conservation and tradition. All of these poles of these traditions, matter... We evolved as much as social beings as we did as individual beings. We evolved as much in laying down the foundations for a stable society as we did in continually pursuing novelty... The consumer economy', Jackson concluded, 'has preferenced novelty-seeking selfish behaviour because that is what we need to keep the system going.'

Jackson quoted French President Sarkozy, launching the Commission on the Measurement of Economic Performance and Social Progress: 'The financial crisis doesn't just free us to imagine other models, future worlds. It obliges us to do so.'

David Brooks, political analyst for the *New York Times* and PBS NewsHour (Brooks 2011) pointed to the contribution of geneticists, neuroscientists, psychologists, sociologists, economists, and others over recent decades who have made great progress in understanding the inner working of the human mind... 'The cognitive revolution of the past 30 years provides a different perspective on our lives, one that emphasizes the relative importance of emotion over pure reason, social connections over individual choice, moral intuition over abstract logic, perceptiveness over I.Q.'

Sociologist James March observed some time ago, rather than making rational choices people indulge in normative decision making: they ask what sort of person am I, what would a person like me do in a situation like this, and they do it! (March 1982).

2.7 Reciprocity

Researchers at the Economics Program and the Program on Cultural and Social Dynamics at the Santa Fe Institute studied the way people deal with reciprocity, the response to gift giving and the extent to which obligations are created through that (Heinrich et al. 2005). Using well-known games to explore co-operation they studied the way in which self-interest works, or doesn't, in 15 small-scale

societies—most of them indigenous—around the World. Together they exhibit a wide variety of economic and cultural conditions.

In one game (called Ultimatum), a ‘proposer’ was provisionally assigned an amount of money or equivalent goods equal to a day or two’s wages and makes an offer to the ‘respondent’ who may accept the proportion offered or reject it. If accepted the players receive the proposed amounts, if rejected they receive nothing. The market economic model, based on the primacy of self interest, would predict a high rate of rejection of any offer significantly less than half the available amount. That has been found in experiments in advanced societies where such offers are rejected and so neither of the participants gains a reward.

In small scale societies participants’ reactions reflected the everyday reactions reflected the everyday situations with which they were familiar. Most offers were accepted so long as they were at least a quarter of that available; generous offers were rejected where it was considered that unreasonable reciprocal obligations in future encounters would be created. The wide variation in the behaviour reflected the extent to which the different societies were involved in regular sharing and trading situations, that is the extent to which the market was integrated into their activities.

Many people respond to nice behaviour of others by being nice to them and more cooperative. ‘Conversely, in response to hostile actions they are frequently much more nasty and even brutal’ (Fehr and Gächter 2000a, b). Moreover, ‘free riding generally causes very strong negative emotions among co-operators and there is a widespread willingness to punish the free riders.... this holds true even if punishment is costly and does not provide any material benefits for the punisher... the more free riders deviate from the cooperation levels of the co-operators the more heavily they are punished. They can avoid or reduce punishment by being more cooperative. Punishment opportunities lead to less free riding.’

Studies of the behaviour of Capuchin monkeys reveal loss aversion, a tendency to choose strategies which result in minimal loss over those which result in greater losses even if they also result in greater gains (Chen et al. 2006). This behaviour is part of ‘Prospect Theory’ as developed by Amos Tversky and Daniel Kahneman.

Neoclassical economics posits that financial incentives drive improved performance. However, this is not so in all domains in all situations. It is fair to say that billions of dollars have been wasted by governments and business in paying huge bonuses to executives, all justified by the assertion that it is necessary to attract the best talent! In some years the bonuses were so substantial that they raised the index of inflation leading to a rise in interest rates which impacted less advantaged people.

2.8 Mirror Neurons and Belongingness

Humans are inherently social animals. Social research shows concern for others to be a major feature of humans and indeed many other social animals. Studies of so-called mirror neurons which fire when the animal acts *and* when it watches another

animal performing the same act strongly suggest facilitation of social behaviour and very likely empathy. Mirror neurons were first found in the ventral premotor cortex, an area near the front of the brain, of macaque monkeys by scientists at the University of Parma in Italy. Subsequently, in April 2010, scientists at the University of California Los Angeles reported mirror neurons in other regions of the human brain, those involved in vision and in memory (Anon 2010). Other social animals show evidence of concern about the welfare of others of their species but in humans this characteristic is much more developed.

Distinguished neurophysiologist V.S. Ramachandran of the University of California San Diego considers the elucidation of the role of mirror neurons will ‘do for psychology what DNA did for biology’ providing ‘a unifying framework and help explain a host of mental abilities that have hitherto remained mysterious and inaccessible to experiments including the development of tools and of speech, amongst other things’ (Ramachandran 2000).

Numerous other studies support these conclusions about the sociality of humans. Roy Baumeister of Western Case University and his colleague Mark R Leary (Baumeister and Leary 1995) concluded that evaluation of the empirical literature supports the proposition that there is a need to form strong, stable interpersonal relationships. ‘Belongingness’ as they call it, appears to have multiple and strong effects on emotional patterns and on cognitive processes. Lack of attachments is linked to a variety of ill effects on health, adjustment, and well-being.

2.9 Neoclassical Economics: Adam Smith Made Small!

Economists, and politicians, like to refer to Adam Smith, the eighteenth century Scottish philosopher and author of *The Wealth of Nations*. Smith, they say, considered freedom to pursue one’s own self-interest to be one of the three things that make us more prosperous, in a general sort of way. (The other two were specialization, which Smith called division of labour; and freedom of trade: Smith was an ardent anti-mercantilist.) Amartya Sen points out Smith was concerned not only with the sufficiency of self-interest at the moment of exchange but also with the wider moral motivations and institutions required to support economic activity in general. Sen (2010) observed, While some men are born small and some achieve smallness, it is clear that Adam Smith has had much smallness thrust upon him.

When Smith referred to self-interest what he meant was that it was a good idea for individuals to try to better themselves: Smith was writing in a time when the overwhelming majority of people were living in extremely poor conditions in almost every way. To give self-interest the emphasis it is given today—a kind of Darwinian survival of the fittest—is to completely ignore the context in which Smith wrote. Smith did not mean to imply an emphasis on the individual to the exclusion of others; he did not mean that competition should be the driving force of the human condition.

American writer and satirist, and biographer of Adam Smith, P.J O'Rourke, talking on NPR Radio's Talk of the Nation on January 8 2007, pointed out, that in the chapter 'Of the Wages of Labour', in book 1 of *The Wealth of Nations*, Smith remarked in a tone approaching modern irony, 'Is this improvement in the circumstances of the lower ranks of the people to be regarded as an advantage or as an inconveniency to the society?'

'Smith wasn't talking about Gordon Gekko in Wall Street, laughs O'Rourke, He was talking about poor crofters in Scotland. At the time he was writing, the majority of people the world over had no capacity to exercise self-interest. They were serfs, slaves, peons working for pitiful wages. All their behaviour was subject to the will of others.' (Walsh 2008). By self-interest, Smith meant having a chance to better themselves, to improve their standards, have the liberty to start a business without interference by the rich and powerful.

In an extensive critique of the way in which contemporary economics has diminished modern humanity, historian Tony Judt (2009) notes that Americans would like their child to have improved life chances at birth, their wife or daughter to have the same odds of surviving maternity as women in other advanced countries as well as full medical coverage at lower cost, longer life expectancy, better public services and less crime.

When told that these things are available in Austria, Scandinavia, or the Netherlands, but that they come with higher taxes and an 'interventionary' state, many of those same Americans respond: 'But that is socialism! We do not want the state interfering in our affairs. And above all, we do not wish to pay more taxes... it is incontrovertible that social democracy and the welfare states face serious practical challenges today'.

Judt points to 'remarkable achievements' to the credit of the welfare state such as, in the case of the neo-Keynesian governments of the postwar era, their success in curbing inequality. 'With greater equality there came other benefits. Over time, the fear of a return to extremist politics—the politics of desperation, the politics of envy, the politics of insecurity—abated.' But, Judt observes, the reasons for the welfare state had been forgotten by the 1960s and it was all neglected by the 1970s.

2.10 The Consequences for Education

Neoclassical economics has become the driver for education policy in countries such as the US, UK and Australia, as well Norway and Italy and some other countries including recently to an extent, Sweden. This has meant, at the very least, advocacy of performance indicators in the form of standardised test scores, merit pay for teachers (based on students' test scores), choice through independent schools and oversight by community representatives on school boards. In some cases, for instance in England, business enterprises now manage schools and provide basic services.

The benefits of education to the community at large from advanced education are ignored as is the fact that development of teachers' expertise is not acquired in a few months from the time the need for such expertise is acknowledged. What is also ignored are the many apparently successful experiments in education of less advantaged students, in the US for instance. Rather, the views of those people which conform to neoclassical ideology are promoted. For example, much attention was paid in Australia shortly after the election of the Rudd government to the views of media magnate Rupert Murdoch and the then Chancellor of the New York school system, Joel Klein, as reported in the Introductory essay to this book. Little attention was paid to the views of experts from the UK such as Cambridge University Emeritus Professor Robin Alexander, principal author of the Cambridge Primary Education Review established by the UK government or Sir Ken Robinson, one time chair of the National Advisory Committee on Creative and Cultural Education, also established by the UK government.

Sometimes, neoliberal views which intrude upon the education scene, especially at school level, are referred to under the heading of 'New Public Management' (NPM). In all cases, the introduction of NPM has generated tensions between education as a social good and as something freely available to all and the notion of schooling as a commodity, its utility measured by the extent to which it prepares students for work and is accountable for the extent to which it does so.

These tensions have been studied in a number of countries including the UK, Norway and Italy (Hall et al. 2013). In the UK, specifically England, NPM has severely weakened the former basis of education over several decades including particularly during the time of the Blair Labour Government. England is now appropriately described, according to David Hall and colleagues from the University of Manchester, as having a 'post-welfarist' public education. Education is regulated in order to provide performance data that serve education markets and is viewed as being about 'passing on the correct knowledge and moral values to future generations'.

In Norway the main tensions are between education as underpinned by socially democratic ideologies linked to notions of equity, participation and comprehensive education and competition, marketisation and privatisation; conservative parties seek to privatise education whilst opposing political parties seek to overturn such trends, according to Jorunn Møller and Guri Skedsmo of the University of Oslo (in Hall et al. 2013). The professional autonomy of teachers has been overturned and principals are seen as managers. In Italy, tensions are manifested as struggles between managerialist accountability and performance control on the one hand and welfarist arrangements on the other, according to Emiliano Grimaldi and Roberto Serpieri of Naples' University Federico II (in Hall et al. 2013).

What seems to not be obvious to those advocating these reforms is that whilst they promise more freedom from control they produce more bureaucracy and centralised direction. Even worse, far from leading to improvements in education, they diminish the outcomes. As elaborated elsewhere, education, especially schooling, becomes nothing more than a process for producing people suitable for basic tasks in enterprises dominated by routine where on the job training is

minimal because the expectation is that people will arrive to be recruited fully equipped. Should they not be, then clearly the education system is at fault and greater accountability is required to fix it up. And more didactic teaching is required, not the student-centred approach advocated by so many. Arguably, the entire notion of neoliberalism and NPM is a fraud!

Reforms of education in those countries whose students perform well in international tests—Finland, Korea, Singapore, provinces of Canada such as Ontario and so on—do not follow these prescriptions. These are issues taken up in other essays, especially as they relate to effective teaching and learning and the conditions of employment of teachers.

In the end, what has neoclassical economics and NPM contributed to the advance of society and education over the last 60 years of extraordinary focus on economics combined, in some countries, with a neoconservative approach to politics exemplified most especially by the US but in many European countries as well? Some commentators, such as one time advisor to the President of Estonia and Senior Legislative Analyst in the US Congress Wolfgang Dreschler (2005) and London School of Economics Professor Patrick Dunleavy (Dunleavy et al. 2005), have pronounced NPM to be dead: their judgements unfortunately have been premature!

Many economists point to the millions in some countries lifted out of poverty over the last several decades. But against that must be put the millions still living in poverty in India, sub-Saharan Africa and South America, the failure of developed countries to meet the Millennium Goals and the increasing disparity in wealth in many of the most highly developed countries, termed by Paul Krugman the Great Divergence. One detailed analysis has concluded that the exploding rise in wealth by a tiny percentage of the population has been due mainly to various failures in the education system and political influence—Wall Street and corporate boards' pampering of the Stinking Rich in particular deregulation and lowering of taxes followed by limitations on unions or decline of labor but not immigration, race or gender or computers (Noah 2012).

Considerable attention has been paid to the recent study of the origins of power, prosperity and poverty by MIT economist Daron Acemoglu and Harvard political scientist James Robinson (Acemoglu and Robinson 2012). Their thesis, supported by analysis of societies from Roman times to the present is, No society which organizes the economy to benefit just 10 % of the population will generate prosperity. To grow and become prosperous the most critical thing a society must do is to harness its talent and human potential which is widely disbursed in the population.

2.11 The Irrelevance of Market Economics

Academic economists have focused on refining econometric analyses for which there is substantial data rather than rare events concerning human behaviour which have very important, often negative, consequences. All the evidence from studies

of behaviour, sociology and neurobiology shows humans to be anything but the utility maximisers, money-driven individualistic creatures that neoclassical economics posits.

Markets are not the efficient mechanisms claimed for them. Continuous economic growth is unsustainable. Increasing the wealth of the already rich does not increase overall prosperity. Privatisation of government assets and functions have replaced public monopoly with private monopoly and produced no greater efficiency.

Government and the private sector together generate prosperity and are involved in a complex system of mutual independence. Provision of social services by government in Nordic and European countries has led to more equitable societies.

Will Hutton (2012b) of *The Guardian* has recently pointed to the failure of the three interlocking pillars of British capitalism. Editor in Chief for the Australian online magazine *Business Spectator* Alan Kohler (2012) reported a major business conference as delivering one overriding theme—that most of the world, if not all of it, is now governed by rich elites who are just out to look after themselves—oligarchies.

Joseph Stiglitz in his new book *The Price of Inequality: The Avoidable Causes and Invisible Costs of Inequality* describes how unrestrained power and rampant greed are writing an epitaph for the American dream (Roberts 2012). Stiglitz writes, ‘Paying attention to everyone else’s self-interest—in other words to the common welfare—is in fact a precondition for one’s own ultimate wellbeing... it isn’t just good for the soul; it’s good for business.’

Social scientist Robert Putnam, author of *Bowling Alone* about the increasing move away from social activities reveals, according to Will Hutton, that class is becoming ever more important as a determinant of outcomes in American life; it now trumps race, he argues, and the differences can be observed very early on in the children of different classes (Hutton 2012a). The middle class now spends more on children’s enrichment activities, so important for psychological wellbeing and character building, in fact 11 times more, than families at the bottom.

Harvard philosopher Michael Sandel has pointed to everything being priced and commodified: ‘We have drifted from a market economy to being a market society.’ (Aitkenhead 2012).

That regular economists whose forecasts of economic indicators seem irredeemably wrong continue to be heard is surely a matter of great concern. Of even greater concern is the fact that much attention is paid to proponents of the current orthodoxy, whilst the fact that the basis of many of their judgements such as the relationship of debt as a proportion of Gross National Product to future economic growth turn out to be based on simple arithmetic errors (Krugman 2013) are glossed over and the fact that many academic economists chose not to explore the difficult issues of economics are not even mentioned publicly!

Distinguished American author and columnist William Pfaff, reviewing Francis Fukuyama’s *The Origins of Political Order: From Prehuman Times to the French Revolution*, wrote, ‘I am not myself aware that human character and conduct today

display any general improvement over that recorded in the historical past. That men and women are morally improved from what they were at the beginning of recorded history has yet to be demonstrated.’ (Pfaff 2011).

Propositions inherent in neoclassical economics, with its focus on maximising utility and the primacy of financial rewards as a major motivator that are predicated on the treatment of humans as competitive, self-regarding creatures are at complete variance with all the evidence from behavioural economics, psychology and sociology. Studies of reciprocity, mirror neurons and belongingness and many other studies show, as Tim Jackson says, ‘We evolved as much as social beings as we did as individual beings...’

The adoption of neoclassical economic models and their outgrowth—neoliberalism and New Public Management (NPM)—has played a major part in undermining the attempts at reform of education in a number of countries including Australia and some countries in Europe, but most especially the US and the UK.

Progress in education reform will not be achieved whilst neoliberalism (and NPM) prevails. Politicians, often with the help of sections of the media and with the support of some sections of the business community, lack the preparedness to honestly address the continually emerging understanding of teaching and learning and the nature of effective organisations including the nature of genuine and authentic school leadership!

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