

*the irrationality of  
homo œconomicus*

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HERMAN E. DALY

*As his two preceding lectures have indicated, Herman Daly is sharply critical of attitudes in the economics profession. In this interview with an American journalist, Karl Henson, in 1995, he spells out his criticisms in some detail.*

**KH:** Is the intellectual higher ground in economics increasingly up for grabs?

**Daly:** Good question. My hope is the answer's 'yes'. And in the long run I think the answer is yes. But currently academic economics is quite dismal. University departments of economics are just wasting everyone's time. That's harsh but I think there are some interesting problems, that might otherwise have been dealt with by economics, that don't go away just because economists say, 'Well, that's not economics ... that's ... economic policy or environment or something else.' So they keep themselves exceedingly pure just working out the logical implications of what they have taken to calling the 'canonical assumptions', which is a revealing phrase.

There are certain canonical assumptions which define what it all is, and then you play games and [make] logical derivations on those assumptions. And the world and its real problems are just sort of left to one side. And if you try to apply any of that to the real world it's a real problem because you've abstracted from what are the most important things. The first thing the canonical assumptions abstract from is any notion of community - nothing but isolated individuals, Homo economicus. Community both in the social sense of our identities being made up of interrelationships, and community in the ecological sense of mutual dependence of species in the natural world. So in the core of economics, those things are abstracted from.

When you say that, economists sometimes get mad. They say, 'Oh well, look here at this area of environmental economics, it's been developing here. We're talking about those problems.' Okay, they're beginning to. Problems are being forced on them, and so they're making whatever ad hoc adjustments are necessary to try to deal with the problem. But it's not a satisfactory situation. And I think it [the intellectual higher ground] is up for grabs in the sense that it's beginning to be challenged and I think that some of the popes of the profession are getting rather defensive. But it's still the ant versus the elephant. They're still pretty much totally in control of all the major journals and the major university positions, etcetera, etcetera. So it's maybe a little wishful thinking on my part to say it's up for grabs, but I think it will be.

**KH:** Who are the 'popes of the profession'?

**Daly:** Oh my. Well, people like Lawrence Summers and all the Nobel laureates. Robert Solow, Milton Friedman, folks like that. All the faculty of the major universities.

**KH:** I think a lot of people would say you're a pope or upcoming pope of the profession ...

**Daly:** Well, that's interesting. I suppose that whatever influence I have is much more directly on the general public and not so much through the profession. So that the people who would look favourably on me ... Well, I don't know ... It just remains to be seen how it plays out because they're not the people in the positions of power.

**KH:** Okay, if the intellectual higher ground is up for grabs, here's a doozy of a question - what is the answer? Is it ecological economics? Economic anthropology...?

**Daly:** Well that's what John Cobb and I tried to deal with in *For the Common Good* - what if economics is to move away from being a self-centred academic discipline interested only in working out the consequences of its own assumptions and if it's to engage itself more in the world. And we argued that you have to shift from Homo economicus as the isolated individual to the idea of person in community, whose identity is largely a function of his relationships in community with others and with the ecosystem. So that this community perspective of social and ecological interdependence is critical - and for the future. Economists say 'Oh

yeah, well we dealt with that.' But you go and you look at the basic textbooks and you get the standard isolated circular flow of firms to households, of exchange value going around and around. There's no environment. The theorems of underlying supply and demand are purely individualistic. There's no social element in any of it. And so some people will say, 'Oh you're just criticising bad elementary textbooks. I mean, the profession has gone way beyond that.' Well, wait a minute. Where do people learn their economics? All our congressmen, whatever they know they got out of some basic elementary textbook, and what good is it ... Should the elementary textbook be consistent with more advanced economics? And if advanced economics discovers something is wrong, shouldn't that be reflected in the next edition of the textbook? So I don't accept that. I think the textbooks really show you what are the most fundamental positions that the public accepts so that it is quite fair to... I would say that we have to work into economic theory not only the circular flow of exchange value which is important but also this one-way throughput of matter and energy - the digestive tract as well as the circulatory system - because it's that that ties us to the environment. The sources of low-entropy matter-energy, and the sinks for absorption of high-entropy matter-energy. And that has to be built into the very foundation of Economics, Chapter 1. No tacked on at the end of a chapter on Depletion and Pollution as Externalities like 'Oh gee, we never expected this to happen but it did so now we have to say something about it.' It's built into the very functioning of the economic process that we have to deplete, we have to pollute, that we have to keep those two activities within some sort of ecological constraint and what those constraints are affects the optimal scale or size of the total economy relative to the environment. And that big question has been completely left out. There's no concept of an optimal scale of a total macro-economic system relative to the larger ecosystem. And that fundamentally we have to bring into economics along with the standard questions of allocation and distribution. Some people are beginning to see that, others are really resisting it. So it's strange. The International Society for Ecological Economics - although there are a lot of different opinions there, I think it tends to cluster around the vision which I just stated. There's another group in Sweden, the Beijer Institute for Ecological Economics, which much more leans toward standard economics. They are recognising that there are real problems of dealing with the environment and that maybe standard economics hasn't done enough in that direction, but they have a great deal of faith that the same basic paradigm will function in that direction. So that's a tension. On the one hand, you have people who are fundamentally standard economists but they say 'Oh here's a set of problems we do need to think about a little more.' And then another group of people who say you really need to change your whole way of looking at things in order to adequately deal with those problems. So there's that tension, and it's a very

difficult tension. Because on the one hand you don't want to alienate people, you want to talk to economists, you want to build bridges with economists, you want to bring their talents to bear on important questions. On the other hand, you don't want to be co-opted and swallowed up and have the basic important issue reduced to something that's not so important and fails to see the point and doesn't really engage the issue and sort of co-opts things. So it's a difficult tension.

**KH:** Why is free trade necessarily bad for the environment? ...

**Daly:** My problem with free trade is partly due to the environment - but it's larger than that. I think it's a bad social policy and bad environmental policy. By free trade, what I mean is deregulated international commerce. So the opposite of free trade is not autarky or no trade. The opposite is not state trade or total monopolisation of trade. The opposite of free trade, which is deregulatory, is regulated trade. Trade which is regulated in the national interest by governments involved. And the notion that there should be no national interest [in] this trade across national boundaries, that the state has no interest in this, that this should be left entirely to the mutual benefit of the trading parties ... I mean imagine if this logic were applied say to corporations - individuals within corporations just trade with each for their own mutual advantage - nonsense! ... Every deal that corporation people make has to be vetted up through higher authorities to make sure that it's really in the

interest of the larger entity. And so I think the same thing is the case with trade across national boundaries. The reason again goes back to community because if you have the free flow of goods and capital and, increasingly, labour across national

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boundaries, then you really lose any possibility of policy at the national level. You can't have an interest rate policy that's different from your neighbour because capital is mobile. You can't have environmental cost internalisation standards that are different from other people because if you have higher standards that'll raise your prices higher than your trading partners', and you put your own people at a disadvantage. So you have to have some equalising kind of tariff. So the argument is not that there should be no trade. Trade can be very beneficial. But the argument

is that trade should not be based on standards-lowering competition. You have to maintain certain standards. And standards-lowering competition can be weakening the environmental standards to give cheapness, weakening social insurance standards and safety standards to get cheapness. Weakening standards of child labour ... throwing in prison labour even, [about] which even GATT says, 'Prison labour is too much, we'll retaliate against that.' So I think maintaining these social standards which have been actually hard-won over many years - I mean the length of working day, that's been limited; child labour, these sorts of things. You can make products cheaper if you lengthen the working day, if you employ children ... and so I think there has to be this national community protection of basic standards. We can't allow that to be competed away in the name of free trade. Interestingly, the classical doctrine of free trade as it came from David Ricardo is much more in line with what I've just been saying because in that system, capital did not cross national boundaries. Capital stayed at home and labour stayed at home. The only things that were traded were goods. So you really did have a much more community/national orientation. You have national capital co-operated with national labour - albeit with class conflict, the national community was able to contain that class conflict. You had national labour and national capital co-operating to make national goods, and those goods that competed internationally with other countries and their teams. Nowadays that's all gone, nowadays you have free capital mobility and so you have a capitalist of one nation [saying] to the labourers of that nation, 'Sorry guys, we live in a global economy, I can employ labour at one-fifth of what you want and I can bring the product right back here and sell it, so you guys are out of line, too bad.' And the labour comes back and says, 'Well gee you know, there are bonds of national community.' 'I just told you we live in a global community. All that stuff is over with. All that old national stuff that caused wars. We live in a global economy. Everything is going to be peace now. Don't you want the Chinese labourer to be as rich as you are - are you a racist?', and on and on. So this idea of mutual responsibilities in a national community [is] being dissolved by this idea of the global world economy. We have a global community now superseding the national community - that's passé, now it's global community. That sounds good if you say it fast enough and don't stop to think about. But it's empty. There is no global community. Where community really exists is at the national and subnational level where people take on mutual responsibilities for each other. Not at the global. Now maybe someday there will be a global community. But our view - of John Cobb and I - is we're all in favour of global community, but it would have to be a federation of strong national communities - a community of national communities. And the present vision is not of a federated community of communities, the present vision is of a cosmopolitan world without borders in which you erase national community and replace it with

this globalise single sort of tightly integrated world community. So the vision of a globally integrated economy is really a single system. You have one tightly integrated system that's mutually dependent across the globe. That's a very dangerous kind of system - something goes wrong, you're in big trouble. We prefer nations to be much more fundamentally self-sufficient, not totally self-sufficient, that's too expensive.

*To the degree possible, strive for self-sufficiency.*

But to the degree possible, strive for self-sufficiency and maintain loose international trading relations to make up for where it's hard to be self-sufficient. I mean everyone can make their own aspirin and matches, you don't need to trade multinationally for that. But there are some things that you do need to trade for. That's kind of the vision that we put forward, and you maintain more local control over your economic life. If you don't, then control is shifted far away and the foreigners who control the capital investment in your country may be lovely decent people, they may even be nicer than the local people, but they're far away and they don't really know or have an interest and a feel for what happens there. This is a vision that John Maynard Keynes expressed very similar kinds of notions [to] when he wrote on national self-sufficiency, and his views along with the others have kind of been swept aside in this globalisation mania, which really serves the interests of the global multinational corporations because what holds them in check is the nation state - the rules of the nation. So if they can sort of weaken the nation and play off one against the other, then they don't have any real restraints. ... The other way of controlling international capital would be to have international government and some people advocate that. I see that as frightening. International government. Some things have to be international, for example, we have to deal with global CO<sub>2</sub> and things [like that] at a global level. But again that has to be a federation of national governments because once you have a treaty for global CO<sub>2</sub> or something, who's going to enforce it? It has to be the national governments who signed the treaties. They have to be strong enough to enforce within their own boundaries the conditions that they agreed to in the international treaty. And if capital, labour and goods flow freely across their borders they don't have any basis for exercising the control that they agreed to. Long-winded answer, I'm sorry.

**KH:** Regarding World Bank leadership ... should economists continue to dominate affairs at the Bank ...?

**Daly:** ... I think economists exercise too large an influence at the World Bank. ... You might think of the Bank as kind of the functioning church in the world out

there trying to do good in the world. And the economists at the World Bank all went to seminary and learned their theology and they're trying to apply that theology in the world to do good. Well I think they learned bad theology. I think the seminaries were teaching bad theology and that takes us back to the first point about the intellectual high ground in economics. All economists who work at the World Bank, whether they're from Africa or California, I mean they got their degrees from Harvard, MIT, Oxford, McGill, you know all these top-rate universities across the world, which all teach pretty much the same thing. And so that's their view of the world. And, give 'em credit, they're very often wonderful people trying to do good in the world on the basis of what they know and what they've been taught. So I think the real problem goes back to the academic departments of economics which are supplying the World Bank economists and which are still directly supplying advice to the World Bank. And of course since the World Bank is populated by the products of these places, they're eager to receive the advice from them, and I think that's a fundamental problem. Now, since I pick on economists so much I should say though that when you look around, is there some other discipline that's better? ... for development decision-making. That tends to make me a little more appreciative of economists because the problems that I've been criticising economists for are problems of the disciplinary structure of knowledge. And that's not just limited to economists. All universities have this disciplinary structure in which the discipline is defined in its own terms, in an inward-looking way. So while I would like to see more influence of sociologists and anthropologists and certainly ecologists and environmentalists at the Bank, I wouldn't want to turn it all over to them. I wouldn't want any of those disciplines to be as dominant as economists are. So I guess my argument would be for a more diverse set [of] disciplinary backgrounds. I wouldn't want to replace economists with sociologists. I don't think that would do the job. On the other hand, I think a greater influence of sociologists and especially ecologists and environmentalists at the Bank would be absolutely needed.

**KH:** If economics has been so successful because of the tools it has given people to make decisions, what new tools do you think should be added to the development decision-maker's tool kit?

**Daly:** I like your questions. That one's a ... I think economics has been very successful in one very important area: allocative efficiency. So that [regarding] the efficiency of allocation of scarce resources among competing ends, economists have preached the importance of decentralised decision-making co-ordinated by markets and the price system. This has historically dramatically proven to be much better than central planning in this collapse of the former Soviet Union and so

forth, [and] is something that needs to be recognised and taken seriously. As far as market control of allocation of resources [goes], I think economics has provided a whole lot. And good reasons were given for why this is so. Now, my problem is that allocation is only one fundamental economic problem. It's important, but it's only one. There are two others, which I mentioned briefly before: there's distribution and scale. So allocation is about how resources get divided up among different users - how much goes to produce bicycles, how much to cars, how much to houses. You know, is that efficient given what people want and their ability to pay. You end up giving people the most that you can get of what they want with the resources available. That's a question of efficiency - are allocations efficient or inefficient? The distribution question is a question of justice. Who gets all the stuff that was produced. Does it go to you or me. And that's a question of justice - is it fair, is it a fair distribution? And then the third question of scale - the total amount that gets produced in all of the resources and the depletion and pollution generated by the use of those resources. Is that at a total scale which is within the absorptive and regenerative capacity of the ecosystem? Or are you destroying natural capital at a rate which is too great? The welfare effects of destroying natural capital may be greater than the welfare benefits of what you produced. And whose products required the destruction of that natural capital? So just from a purely anthropocentric view, not giving any value to other species or nature intrinsically, just as an instrument for human betterment, you still run into this limit of scale. So I think those are the two questions which economists have not dealt with. They have logically recognised the necessity of the distribution question and so standard economic theory says that all theorems about allocative efficiency pre-suppose some given distribution, which may be just or unjust. They recognise that, but they don't emphasise it. It's there but it's not front and centre.

*Economics has been negligent regarding distributive justice and extremely negligent regarding optimal scale.*

And the scale question is not even recognised. That's off the radar screen. And to the extent that it's recognised, well it's just a matter of property rights - 'If we just get prices better in property rights, then the problem disappears. It doesn't matter if we grow more as long as we pay the costs of growing more.' So my view is that while economics has done a great deal in the matter of economic efficiency, it has been negligent regarding distributive justice and extremely negligent regarding

optimal scale. So those two things are where the effort should go. We've pretty much given good answers to the allocation problem, I don't think we need to spend time and effort proving once again that the market is efficient, investigating every possible variation. I mean okay, there's room for people who are interested in that, I mean fine, I don't want to tell people what they should do, let people study that. But socially, I don't think that's where the big payoff is right now because past success in that has been impressive, and we need some success in the areas of distribution and scale and that's where we need to devote the effort.

**KH:** Can you think of any particular tools in those areas which you take a shining to?

**Daly:** I think that yes, there has been an evolution in policy which has forced us to deal with the scale question. And that has been in things like the bubble system where [there are] marketable licences to deplete or pollute. And these kinds of policies are excellent because they clearly say the first problem you have to solve is the scale problem - what's the total amount of emissions that are acceptable in this watershed or airshed or county or whatever. The second question is, given that there's that total limit, that means it's no longer a free good, that means it's valued: the distribution question - who owns it. You've created a new asset which is now limited - who owns it? Shall we give it equally to all citizens? Shall we give it historically on the basis of who's been using it most? So you have to face the question of fairness of distribution. And then in third place - after you solve the scale question, on ecological grounds presumably, after you solve the distribution question, on equity grounds presumably - only in third place is the market trading allowed to solve the allocation question and efficiency. So I think that [has] provided a way of moving in the policy area ... And since it seems to have evolved pragmatically, I think it's way ahead of a lot of standard economic theory. It just sort of pragmatically brought in scale without creating a big fuss about it. ... And of course population issues, we have to deal with population limitation and that's been a long and heated subject but I think we do need to deal with that much more forthrightly. And well the scale question - that's part of the scale question of population times per capita resources or total resources. So one way of reducing scale is dealing with population, the other way is per capita consumption. So both of those I think are important. So in the North we have to focus more on limiting our per capita consumption. In the South I think the focus has to be more on limiting numbers. And that might be the basis of a kind of North-South bargain. Because currently it's very difficult for the North to tell the South you should limit your numbers so you save all these resources that we can gobble up in over-consumption. And it's also difficult for the South to say to us, you should limit

your per capita consumption and save these resources so we can dissipate them all in population growth down here. So it seems to me there has to be some basis of a global agreement or compact. And that idea of limiting scale, by operating both on population and per capita consumption is to my mind a reasonable possibility. But I don't mean to tell you that's it's not something that popular, it's certainly not popular. The other thing I would mention in addition to this tradable permits notion and that some of us are pushing right now ... given the political climate, probably the best thing that we can pray for is ecological tax reform. Shift the tax base from income, labour, value-added onto that to which value is added - namely the resource flow. So tax throughput, tax depletion and pollution, tax the resource flow - that to which you are adding value. That is what's causing depletion and pollution. Those are 'bads'. Tax bads, stop taxing goods. That's the basic idea. You don't want to tax what you want more of. You do want to tax what you want less of. This could be sold as a revenue-neutral shift. We're not going to tax more, we're going to tax differently, we're going to tax different things to instil different incentives. And the incentives that result from this would be not to dampen the incentive to work or to accumulate capital or to improve it, but to dampen the incentive to use more resources. So we would then collect money from the resource flow, which is what is tightly associated with depletion and pollution. And that would I think be a move toward efficiency, and standard economists agree with that to a large extent. It's kind of a political movement. In Europe, in Germany, Ernst von Weizsäcker and others have pushed this idea very strongly and I think convincingly. So it seems to be kind of the one policy I can think of now which in a conservative political time might have some political chance of being considered, and yet which could still have some real bite, some real effect. Now, some people would immediately say that it's very optimistic to think that it's politically feasible ... given our recent experience here [in the US] with an attempt to pass a gasoline tax. So this would be kind of [a] gasoline tax writ large on all resources. Well you know, maybe so. It wouldn't be politically easy, but it does seem to me that it's in the realm of feasibility. There's so much logic to it, and I think your neo-classical economist [and] your ecological economist pretty much are in agreement that this would be a good sort of thing.

**KH:** Re revenue neutrality - not within a sector?

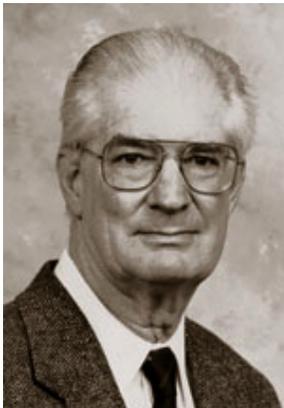
**Daly:** Absolutely. It would be revenue-neutral only in an aggregate sense that the government raises the same amount of revenue. By raising it differently it would impinge on different groups differently so that you might say that everyone would benefit by a reduction in income tax and everyone would pay more in resource taxes. However the next balance in each case is going to be different. Some people

or some interests may consume a whole lot of resources, and so there would [be] a shifting incidence - the incidence would fall differently, so I think that probably initially to gain political acceptance there would have to be some compensation for the differing incidence. So maybe corporations who are adversely affected by the shift would.....maybe they would get a little greater forgiveness on income taxes or something. But those are important questions that have to be worked out, it's pretty hard to know exactly what this incidence would be. And one would have to move towards it gradually, a certain amount each year. We couldn't just do an abrupt, all-at-once shift. It would have to be a gradual thing which would give people a chance to see what's coming and adapt to it before it hits, and make their adjustments.

**KH:** Thank you very much.

**Daly:** Thank you.

*This interview was conducted at College Park, Maryland, USA on February 8, 1995. It first appeared in Developing Ideas.*



### **Biographical Sketch :**

*Herman E. Daly is currently Professor at the University of Maryland, School of Public Affairs. From 1988 to 1994 he was Senior Economist in the Environment Department of the World Bank. Prior to 1988 he was Alumni Professor of Economics at Louisiana State University, where he taught economics for twenty years. He is co-founder and associate editor of the journal Ecological Economics. His interest in economic development, population, resources, and environment has resulted in over a hundred articles in professional journals and anthologies, as well as numerous books, including *Toward a Steady-State Economy* (1973); *Steady-State Economics* (1977; 1991); *Valuing the Earth* (1993); *Beyond Growth* (1996) ; and *Ecological Economics and the Ecology of Economics* (forthcoming). He is co-author with theologian John B. Cobb, Jr. of *For the Common Good* (1989;1994) which received the 1991 Grawemeyer Award*

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