# Book Reviews

**The Moral Economy: Why Good Incentives Are No Substitute for Good Citizens.**

Samuel Bowles. 2016. New Haven, CT: Yale University Press. ISBN 978-0-300-16380-2, $27.50.

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Samuel Bowles does important, creative work at the intersection of economics and the behavioral sciences. In this book, he draws on the innovative literature across this boundary to argue for a new policy paradigm to replace the highly-developed "constitution for knaves" that dominates current economic policy. He does not advocate abandoning the employment of incentives and the assumption of self-interest, but wants to enrich the policy story by adding ethical and other-regarding motives which interact with self-interest and with policy in discernible but complicated ways. Bowles claims that this approach recovers a Humean and Smithian account of policy, and makes economics more useful to politics as conceived by Aristotle. This review will praise *The Moral Economy* for its economics, but criticize its pretensions to a sort of technocratic political philosophy. Bowles does indeed bring together the "moral sentiments and material interests" of Hume and Smith in an innovative synthesis, but his analysis cannot get us all the way to Aristotle's Legislator.

In chapter one, "The Problem with Homo Economicus," Bowles lays out the justification for the assumption of self-interest, and calls it into question. He notes that few researchers, in fact, believe that the assumption is true, but argue that it is prudent to adopt it; it is better to assume that people are knaves and be wrong than to assume they are always good and other-regarding and be wrong. There will be less damage from falsely assuming pure self-interest than from falsely assuming pure ethical behavior.

Bowles notes two problems with the self-interest assumption: policies based on it may erode ethical behavior, and material incentives can backfire. As evidence of the complexity of incentive effects, Bowles cites the Haifa daycare study (Gneezy & Rustichini, 2000), in which an imposition of a fine for late child pickup resulted in an increase in the number of late pickups. The disincentive for lateness was interpreted by parents as a price; the expectation of a market exchange replaced the moral expectation of timeliness. Evidently, in some situations, individuals act in accord with the assumption of self-interest, and in others, they act in accord with the assumption of other-regarding ethical norms. Bowles argues that good policy requires a paradigm shift toward an integrated account of the two types of behavior.

In chapter two, "A Constitution for Knaves," Bowles sketches the history of governance, claiming Macchiavelli, Hume, and Smith as allies. Contrary to popular impression, none of these thinkers assumed purely self-interested motives, but acknowledged that a healthy society and a productive market require a foundation of good customs and fellow-feeling. The law should channel self-interest toward the public good, but it should also seek to foster and safeguard the moral sentiments upon which the economy rests. Economics in the twentieth century did not reject outright the dual nature of the individual, but assumed that moral sentiments and material interests were, in practice, separable. Along with the separation of economic analysis from ethical concerns in the life and work of the economist came an assumed separation of the effects of ethical concerns and self-interest in the lives and decisions of the individuals whom economists study.

The assumption of separability is convenient; it allows the economist to focus solely on incentives (prices and information) and efficiency. As detailed by Bowles, however, moral sentiments and material interests are difficult to separate in practice. The conditions required for efficiency are so restrictive that economists often rely on individuals (including policymakers) to internalize the costs and benefits that are relevant to efficient choice but are excluded from prices by incompleteness in markets and contract.

Bowles spends chapters three through five documenting just how entangled ethical and self-interested concerns are, and the dangers of assuming separability. Chapter three ("Moral Sentiments and Material Interests") draws on several studies across cultures to demonstrate how incentives that address self-interested behavior can undermine (crowd out) other-regarding behavior and norms. Although altruistic agents are not unimportant in these studies, reciprocal behavior on the part of a significant proportion of agents appears to be more important. The disposition to seek cooperation can be eroded when fines are imposed or material rewards given. In light of this crowding out (sometimes, crowding in), the legislator must take into account a more complex relationship between incentives and behavioral outcomes; she must take into account both the effect of the incentive on a self-interested agent and its effect on the proportion of agents who act in a self-interested way.

The phenomenon of crowding out or crowding in demands an explanation: under what conditions is each likely to occur? Can we predict it? Chapter four ("Incentives as Information") explores three ways that incentives may change the frame within which a decision is made, from something more communal and reciprocal to something more self-interested. When the Boston Fire Commissioner threatened to penalize firefighters who exceeded fifteen sick days, Bowles suggested that the firefighters interpreted this as a lack of trust, as a violation of a reciprocal equilibrium, and accordingly took more sick days. In the same way, a fine may lead to a reframing of a moral obligation ("pick your child up on time, so you don't impose on the children and the staff") to a material transaction ("pay extra and pick your child up later"). A fine or a reward may cause those affected by it to conclude that they are being managed or manipulated and to assert their autonomy by resisting or rejecting the desired effect of the incentive.

In light of evidence that incentives may undermine communal norms, an important puzzle remains: Why is there no full crowding out? Why do communal norms resist erosion? In particular, why do market-oriented societies, in which incentives and anonymous transactions are ubiquitous, produce more reciprocal behavior and generosity in ultimatum games, prisoners' dilemmas, and public goods games? To explain this, Bowles makes a couple of distinctions. First, he divides the effects of incentives into long-term and short-term effects. Short term effects are framing effects, liable to change as contexts change, and leaving no lasting effect on moral sentiments. To describe longer-term effects, Bowles relies on more evolutionary language, in which repeated interaction gives rise to more cooperative norms and expectations.

Since most of the research on crowding out is short-term and context-dependent, it does not address the existence of longer-lasting norms, which result from longer-term evolutionary forces. Bowles admits that evidence on these longer-term evolutionary processes cannot be gathered in the laboratory, and so we are reduced to speculation (hopefully, informed). His skeptical response to the "Doux Commerce" hypothesis, which explains cooperative behavior in market societies as a result of repeated interaction and the necessity of trust, is plausible but equally speculative. Bowles suggests that liberal societies (which are usually market societies) provide formal and informal social insurance which protects citizens from the worst downside risks. This elimination of downside risk makes citizens more willing to engage in cooperative behavior by reducing the cost of trusting but being betrayed. This is an intriguing alternative to Doux Commerce, although there is work to be done in sorting out the relative power of the two hypotheses.

I cannot think of a better summary of the growing impact of behavioral research on the way we think about policy than this book. It convincingly argues for a new (or at least more complex) paradigm for economic policy. Well-designed prices do not substitute for moral sentiments. Good policy should take into account the relationship between the incentives and moral sentiments. Both are important, but they interact in important ways.

Although Bowles breaks free of the pure self-interest assumption and the mechanism design challenges to which the assumption gives rise, and thus gives a more complicated account of the challenges of managing the economy, his book falls short of an integrated account of political economy—as a practical manual for legislators. I must emphasize this point, because Bowles clearly has ambitions for something more than a limited economic treatise. Early on in the book he invokes the Aristotelian "legislator," the virtuous ruler who by wise rule and well-chosen laws fostered the happiness of citizens. He describes the "Legislator's Dilemma" in chapter six, and offers the Aristotelian Legislator practical advice in chapter seven.

Indeed, a wise Aristotelian legislator ought to pay attention to Bowles's advice and his framework of analysis; nevertheless, Bowles's invocation of Aristotle (and those who followed him in political theory) is undermined by his determination to interpret them within a purely economic framework. This causes Bowles to overlook important differences in the way that Aristotle conceived of happiness and governance and, consequently, to overlook what Aristotle offers that economics overlooks.

Bowles's work is intriguing because it lays out a richer framework for analysis than those currently on offer from economics; it is an analytical improvement, but it is insufficient for governance and political economy *because it is analytical*. Its limits are the limits of technocratic accounts of practical action. In technocratic analysis, ends are given, phenomena are measured directly or by means of suitable proxies, empirical relationships are discerned statistically, hypotheses are modified or rejected. Policymakers then make use of the established relationships among variables to pull the appropriate levers to get the desired outcomes. This is the method of public policy and economics, but it is also the modern method of engineering, physical and social.

Technocratic approaches to social science and policy provide an exceedingly helpful abstract perspective, a map or blueprint to guide our inquiries. An abstract mathematical model paired with careful and creative empirical work can reveal patterns of causation that are only revealed from a distance. Nevertheless, the technocratic approach is not sufficient for making decisions and acting on them. This should be obvious from the way economists qualify their policy advice in seminars: Something intangible must be added to economic analysis to make policy. Economic analysis is highly contingent: Do the patterns found in one country at one period of time and in one subsample exist in the policymaker's country, time, and population? Are the observed patterns in the data causal? Are the recommended incentives and institutions feasible in the current context? Who are the important policy players, what do they want, and how skillfully do they govern? Are the ends posited in the model the actual ends of policymakers or citizens?

Good policy does not ignore the analytical contributions, but must combine these with an awareness of the complexities of context, and an ability to improvise like an entrepreneur. Good policymaking involves a dialogue between technocratic analysis and the realities of context. The ability to do this well is an embedded skill which is not well-described in technocratic terms. Aristotle would have called it a virtue—the virtue of practical wisdom.

By method, technocratic approaches to governance ignore the embedded virtues by which people make effective policy, in favor of rigorous theory and careful empirical research. The work of combining good analysis with the complexities of context—what ends are worthy of pursuit, how do the models match up to reality, who is making policy and what skills do they bring to their task—is taken for granted in economics or is ignored as irrelevant.

It is easy to get caught up in the enjoyment of creative economic analysis applied to policy, but nevertheless I want to highlight three consequences of the technocratic approach which may go unnoticed. First, little attention is given to the appropriate ends of policy. Take the ubiquitous example of the tardy parents at the Israeli daycare center. The assumed end of the analysis is reducing the number of tardy pickups; the discussion of the felt moral obligation to pick up one's children, which may be undermined by a fine, is purely instrumental. But is nothing lost when parents abandon the more human connection that causes guilt when they are late and communicates respect when they are on time? An Aristotelian legislator might care about more than the on-time pick-up rate, but this would require deliberation (communal or individual) about the value of the community and the ties among its members. Technocratic analysis by its nature must ignore this most important task of a community and its leaders.

This book (like most economic treatises) takes ends resolutely for granted: The Legislator determines to provide some public good and, with the advice of economists, designs institutions to elicit the appropriate contributions to that public good. I do not dispute the importance of this work, but it cannot be said often enough that it is not an adequate description of the task of the Legislator. To imagine that a more complex analytical model gets us closer to a technocratic description of the policymaker's task is to misunderstand policy.

Unfortunately, I get the impression that Bowles thinks that economic analysis can span the practical space within which the Legislator operates. In doing so, he oversteps his expertise and runs roughshod over centuries of careful (and rigorous) work in political philosophy. For example, Aristotle's Legislator (leaders like Pericles, or the ideal of the virtuous philosopher king) is reduced to a skillful manager who acknowledges that citizens respond to incentives in complicated ways. Bowles and the researchers he cites turn Kant's deontological ethics on its head; Kant developed his deontological approach as the product of pure reason free from emotional interference, but here it becomes the product of emotional "affects" which constrain utilitarian consequentialist reason (p. 105). In general, previous political philosophy is treated as if it is not worth the time to refute or reject its categories. Virtue and deontology, as intellectual products of a pre-technocratic era, are treated as seeds of ideas which can only be brought to full flower by rigorous analytic method.

There is no lack of confidence here that what is lacking in policy can be supplied by the new paradigm. In this telling, the shortcoming of the previous, purely self-interested paradigm was not its ambition to reduce policy to pure calculation. All that is needed is a better predictive model from which the policymaker can choose more effective options. Even the potentially ambivalent and unstable nature of social framing can be managed by the efficient technocrat: "He [Aristotle's Legislator] knows that moral frames for social interactions are not difficult either to construct or to suppress" (p. 97).

Perhaps the most important consequence of the purely technocratic mindset that pervades this book is least noticed by economists. The combination of ends fixed or chosen by the Legislator and the emphasis on the causal effects of institutions on human behavior produces a vision of society as something to be managed, something passive which is guided toward ends chosen by the policymaker. It is guidance for shepherds managing sheep; whether the sheep are self-interested or other-regarding matters only insofar as it impedes or promotes the ends of the government. If moral sheep are needed, then institutions can be designed to foster and maintain morals.

I recommend this book for its creative and innovative economic analysis; it moves the field toward a richer and more predictively powerful paradigm. My strong objections are to the book's ambitions to replace Aristotle with social science while failing to understand what Aristotle and the virtue tradition offer that cannot be supplied by technocratic analysis. It is no shame for economists to admit that what they have to offer is insufficient for policy, but all too often economists fail to see what their models cannot capture.

## Reference

**Gneezy, U., & Rustichini, A.** (2000). Pay enough or don't pay at all. *Quarterly Journal of Economics 115*(2), 791–810. ■