

PROJECTING THE NEW ECONOMIC WORLD ORDER

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Values

This sixth ICUS is the first for me; I feel I should begin my paper with a brief confession about the values underlying it. Some doubts I had had about ICUS were reawakened by the summary report of the fifth ICUS. Gratified by a complete identification with the hopes expressed in the introduction by the Reverend Moon that it would contribute to the realization of a "world of happiness, peace and love," I was surprised and slightly disturbed by my complete disagreement with Sir John Eccles' propositions about absolute values and absolute truth as well as with Max Jammer's belief (and apparent regret) that advances in physics have robbed us, allegedly for the first time, of an alleged "coherent and intellectually satisfying world picture." I am in full agreement with W. H. Thorpe's conclusion

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to the report--that belief in a "meaning" of the world, as distinct from scientific understanding, rests on religious faith or on an accepted system of myths. My confession is that I feel no need for a belief in a meaning of the universe or in the existence of absolute or universal values or in the possibility of absolute truth.

Yet I do not feel out of place in this conference because shared values are all that we need for cooperation for the advancement of the human welfare goals raised in the introduction. A search beyond these for absolutes not only takes time and energy away from the goals but carries with it a danger. A conviction that absolute values have been discovered or absolute truth achieved can easily lead, again, to a losing of the human welfare goals in a concentration on the condemnation of "wicked" values and the eradication of heresy.

The mobilization of shared values in the task of furthering human welfare is best served by Occam's Razor: demand only the minimum necessary, require only those essential for cooperation and only those that are needed for the cooperation that is feasible, and be prepared to work only with those who share these values.

### Economics

Having settled the matter of basic values--at least to my own (current) satisfaction, I turn to the basic economics. I do not like the expression "closing the gap" between the rich and the poor since this suggests equal concern for pulling down the rich as for raising up the poor. I am concerned only with eliminating poverty. Taking from the rich (which usually turns out to be mainly taking from the

not-quite-so-poor) can contribute to this end, but any real solution must be found elsewhere. Two basic well-established economic propositions are:

1. Raising the level of living of the poor of the world to any satisfactory standard must come primarily from increased production.

2. No feasible increase in production will be able to provide this for all if the world's population keeps on growing.

A third basic proposition, not so well established, is:

3. Productive efficiency is not enough. Distributive efficiency is just as necessary. Raising productive efficiency alone, leaving unchanged the relative distribution of income and wealth, would be almost completely swallowed up by higher intensities of "keeping up with the Joneses."

#### Productive Efficiency

Productive efficiency is achieved automatically in a free market economic system to the degree that it is perfectly competitive. Government action is required only to correct for imperfections of competition and of the market and to adjust for externalities. Since this "correction" covers all socially beneficial government activity, including the institutions necessary for the market to work, the economic system can also be considered as government planning which only uses the market to correct for bureaucratic imperfections. But whether the capitalist or the socialist language is preferred, it is the market mechanism that achieves productive efficiency. It causes preferred output to be produced wherever possible by shifting productive factors from where the value of their marginal product is

less to where it is greater until the value of the marginal product (VMP) of every factor of production is the same in all its possible uses. Such further improvements are then no longer available.

Productive efficiency is achieved,

There is a value postulate underlying the desirability of productive efficiency:

1. It is better to use resources to produce what the consumer prefers as between different products. But no consideration is given to different degrees of need (for products in general) by different consumers.

#### Distributive Efficiency

The consideration of the degrees of need by different consumers is the province of distributive efficiency. It is concerned with the use of income to satisfy more important, or more strongly felt, human needs rather than less important, or less strongly felt, needs, and it calls for two additional value postulates:

2. All people feel satisfactions or enjoy utilities that are comparable to those felt or enjoyed by oneself and by others.

3. All people rationally choose to satisfy more important needs rather than less important ones at least part of the time.

From these additional utility postulates we can derive the principle of diminishing marginal utility of income. Successive increases in income permit the addition of only less important items since only these still remain to be purchased. From this follows further the basic principle of distributive efficiency:

The efficient distribution of a given income is one that equalizes the marginal utility of income of all the individuals. As long as any two marginal utilities of income are unequal, the transfer of a dollar from where its marginal utility is less to where it is greater will yield a gain in utility greater than the loss. This is an improvement in distributive efficiency. By virtue of the principle of diminishing marginal utility of income it will also lower the greater of the two marginal utilities and raise the lesser one. The continuation of such transfers will continue to improve the distribution but the difference between the marginal utilities will keep diminishing. When this difference has disappeared altogether, the marginal utilities will have been equalized and complete distributional efficiency will have been reached. Of course, this analysis can be compelling only for those who accept the underlying utility postulates--but very few would admit to the arrogance implied in rejecting them.

Distributive efficiency is parallel to productive efficiency. It calls for equalizing marginal utilities of income instead of VMP's. While the market mechanism works automatically towards equalizing VMP's, it does not work at all towards equalizing marginal utilities. Distributive efficiency can be achieved only by governmental equalization of the marginal utilities by redistributing income from where its marginal utility is less to where it is greater.

### Equality

The lack of any objective measure of marginal utility had seemed to block completely any practical conclusions from this approach. But

I have shown<sup>2</sup>, and other economists have shown in somewhat different ways, that a policy guideline can be developed from the utility postulates on which distributive efficiency is based. Every shift of a dollar from a larger to a smaller income entails a probable increase in the utility of the poorer individual greater than the probable decrease in the utility of the richer one. Utilitarian Marginalism thus enables us to derive the policy guideline:

The best that anyone can do who is aiming at distributive efficiency is to spread a given income equally.

But here we meet another obstacle. The distributive efficiency principle seems to be in direct conflict with the productive efficiency principle. The market equalizes the VMP's of productive factors by making these equal to its uniform price. Where the factor is labor, the price of the factor is also the wage, and this serves not only to guide the labor to where its VMP is greatest, but also as an incentive to the worker to provide the service. If equal incomes are provided, there will be no material incentive for the worker to work or for managers to manage, and there would certainly be much less available for distribution. The distributive principle would destroy the productive principle!

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<sup>2</sup>Lerner, The Economics of Control, New York: Macmillan, 1944; "Nozick, Rawls, and Utilitarian Marginalisms," to appear in a symposium on ethics and income distributors in the forthcoming January 1977 number of The Eastern Economic Journal, edited by Professor Raymond E. Canterbury of Florida State University and the late Professor Harry Johnson of the University of Chicago.

This is a misinterpretation. The distributive principle applies strictly only to the distribution of a given income. The argument is valid only as long as a dollar taken from one person permits a whole dollar to be given to the other, i.e., only if the total income is unchanged or "given." But does not this alone suffice to destroy the usefulness of the notion of distributive efficiency?

### "Given" Income

It does not do so because a great deal of the income is "given" in the relevant sense. The prices paid for productive resources have to be as high as the market sets them to discourage their use where the VMP is less than in alternative uses. But there is no need for the owners of the resources to enjoy all such payments as their income. They need get only the payment for that part of the human resources--the work (including the efforts in economical management) which, if not paid for, would have been devoted to the enjoyment of leisure or to more pleasant but less useful work. All the rest is "given." It is available for efficient distribution. Economists of all schools have long recognized this as "rent" or "surplus."

The equalization of the VMPs (for productive efficiency) is indeed achieved by making them equal to the pay. But there is no need for this VMP to be received for all the units of a factor. It is necessary only at the margin. It may seem natural to pay for all the units, but this is only because it is our habit to start counting from zero, and that is arbitrary. We could start counting the daily hours of paid work only after, say, four hours of work had been done. The worker's income would then consist of his equal share of the "social



surplus" plus the VMP of the hours he works in excess of the four hour norm (or minus the VMP of any reduction of hours worked below the norm). The worker would thus be free to work up to the point or margin where his wage (equal to his VMP) just compensates him for the disutility of his work, every employer would maximize the profits of his firm by employing each type of worker, and every other factor, up to the point where the wage or the payment for the factor is equal to its VMP, and productive efficiency would be unimpaired.

#### Degrees of Distributive Efficiency

Distributive efficiency would not be complete, the degree of distributive efficiency depending upon the number of "unpaid hours." The extension of distributive efficiency by raising the norm of unpaid working time (and thus increasing the surplus available for efficient distribution) is limited not by the requirements of productive efficiency but by the willingness of workers to supply the norm of unpaid work for the sake of the pay for work beyond the norm. There is a minimum necessary income without which the worker will not be available for the job. This is determined by the alternative occupations open to him. In a perfectly competitive economy there would be little if any scope for an employer to demand "unpaid hours" (not even from apprentices or medical interns). But where the alternative occupations are similarly subjected to the unpaid norm competition from alternative occupations is easily prevented.

#### Limits to Distributive Efficiency

The effective limit to the equalization of income in accordance with distributive efficiency is not in the necessity of maintaining

productive efficiency. It is in the resistance of workers to equalizations of pay that they regard as "unfair" or as "too socialistic," as below the traditional minimum standard of living for each particular skill or profession required to induce conscientious work.

There is no objective basis for such "required" levels of reward. It is a matter of custom or culture and not of technology. The possible degree of distributional efficiency thus rests entirely on tradition and can be increased as people get used to greater income equality with the moderation or elimination of poverty.

Traditional pay differentials can be protected by political pressures, threats of strikes and most of all by the productive inefficiencies that grow out of feelings of resentment at whatever is felt to be "unjust," and are hard to distinguish from conscious or unconscious sabotage. Only as greater equality of income becomes socially acceptable can greater distributional efficiency be attained. But there is a wide range over which greater distributive efficiency need not damage productive efficiency.

#### Disappointing Slogans

I am now more than half way through my lecture without having even referred to the topic--Projecting the New Economic World Order. But I think that I have laid down some basic economic and moral guidelines, the absence of which has left much of the recent discussions without a proper foundation. The basic intent of the new economic world order is a raising of the economic condition of the poor people of the poorer countries. The Less Developed Countries, LDCs, is the

paternalistic euphemism of the rich countries. The sad observation that successful aid has been the exception rather than the rule led to a turn to the slogan of "trade not aid."

This was understandable as a protest against protectionist restriction of imports from the poor countries with their low wages (inevitable with their low VMPs)--although often weakened by accompanying defense of protectionist restrictions of imports from the rich countries with their low prices (due their high VMPs) which are just as essential for the benefits from trade. But the idea that "fair" trade could cure the poverty of the poor countries is based on the myth that the wealth of the rich countries is stolen from the poor by "unfair" or "unequal" exchanges, rather than produced by ability to make use of technology and of the resources of the earth (including some found in the poorer countries).

Recognition that trade was not enough led to the call for foreign investment which would raise VMPs and wages. But investment is undertaken only if the investor gets some gain from it too, and when a successful investment was completed and the foreign capital returned together with some earnings from the years of the investment, the investors naturally took out of the country more than they had brought in. The poor country's gains had, in some cases, merely increased the number rather than the living standard of the poor. This gave support to the myth that the wealth of the rich was obtained by robbing the poor. Foreign investment, denounced as imperialism or colonialism and discouraged by confiscations petered out before it could lead to successful development as in the United States and Canada.

Another turn was from depending on trade and on foreign investment towards self help, the rich countries only showing the poor countries how to be more productive. This was technical training--Point Four and the Peace Corps--and it too, turned out to be a great disappointment. Many cases of individual devotion and even heroism were sunk in cross-cultural misunderstandings, growing bureaucracy, disruption of cultural systems, and the absence of the infrastructure necessary for economic prosperity.

#### "Fair" Prices

The latest turn is a hope for a New Economic World Order through a reincarnation of "fair prices" as demonstrated by the quadrupling of oil prices by the cartel formed by OPEC, the Oil Producing and Exporting Countries. Although it is the poor countries which are beginning to develop that are hurt most grievously by the increase in the price of oil, and of the fertilizers made with it, resentment at the harm they suffer seems to be more than offset by gratitude to OPEC for having shown them a way of getting higher prices for what they sell to the rich countries while feeling that what they would be getting only is their right by virtue of market power and not from anybody's condescending gifts.

But this is an illusion on both counts. It is doubtful whether the market can be as helpful to any of the poor countries as it has been to OPEC, and it is clear that to many it will be of no help at all.

Conscience Money

In the United Nations General Assembly the poor nations are in the majority, and the rich countries seem willing to make sizeable contributions toward raising the income of the poor countries. But this seems mostly to be taking the form of accepting monopolistic restrictions (which are nothing but the combination of a gift to the restricting poor countries with a damage to world net product) or of gifts otherwise disguised as loans, or investments, or insurance policies, or public relations expenses and by many other aliases. It seems to me that this willingness betrays a vague awareness of the principle of distributive efficiency and a recognition that a large part of the world net product is "surplus," and that its appropriation by the rich is not required for productive efficiency and not justified by the productive efficiency principle. On the other hand, it was never the property of the poor and so it cannot be said to have been stolen from them. Only the distributive efficiency principle gives any indication where it should go--i.e., as surplus which an unbiased distributor would divide equally among all. Much of the income and wealth would therefore have to be transferred from the rich to the poor, but it would not really be given by the rich to the poor any more than it would be given back to the poor by the rich.

International Distributive Efficiency

I happen to be in a better position than most to point out that any new economic order, if it is to succeed in reducing world poverty, must include the sharing of the surplus. In 1945 I proposed that the United States devote 50 billion dollars of its wealth to the

reconstruction of the post war world on a more egalitarian basis. This was considered so naively unrealistic that I could not even get the lecture published for several years until the proposal had been much surpassed by the Marshall Plan and other US economic aid. Even then I could get it published only in the "starry-eyed" Bulletin of the Atomic Scientists.

By 1945 the principle of sharing the surplus more in accordance with distributive efficiency had been accepted on a large scale, but only domestically--for fellow nationals. In the richer countries there were attempts to make taxation of the well-to-do progressive. More successful were some measures for raising the economic welfare of the poor. But the day had not yet dawned for the international application of the principle of distributive efficiency. The earlier suggested bases for the New World Economic Order: the return of riches robbed from poor countries, the dependence on foreign investment, the spreading of technical knowledge, and even the subsidizing of infrastructures, had largely bogged down in bureaucracy, corruption, and disillusionment because a crucial element was missing or underemphasized.

This missing element is provided by the utilitarian marginalism behind the concepts of productive and distributive efficiency. It is the concentration on individuals. It is not nations--the entities mainly dealt with in the earlier approaches--but only individual human beings that have utility and the marginal utility whose equalization, called for by distributive efficiency, is best served by the policy guideline of equal sharing of the surplus.

So thoroughly was this missing element suppressed that attempts by the countries granting economic aid to make sure that the poor people in the poor countries benefitted from it, and not those through whose hands it passed, were denounced as unacceptable "strings," rejected as undermining national sovereignty and attributed to imperialist or colonialist machinations. Even more bitter was the response to suggestions that the aid should be limited to raising the level of living of the poor and not spent where it would only increase their number.

#### Essential "Strings"

The transfer of surplus, to be acceptable and really to increase distributive efficiency, should certainly avoid entanglement with other objectives that might be attractive to the governments of the countries making the transfers. But the "strings" just mentioned are essential conditions for the successful achievement of the New Economic World Order.

Some recent research has shown these strings to be even more essential than appears from the general analysis. Careful econometric studies have shown that even where economic aid has overcome the bureaucratic hurdles, escaped corruption, and resulted in successful development, even where the development disease of poor countries aping the techniques appropriate to rich countries has been avoided, in most cases, more poor people lose than gain from economic development for a considerable time before the benefits trickle down to them. If this is to be prevented, special measures have to be taken to raise the economic level of the very poor before the

development. This further evidence only shows more emphatically that the only consistent moral and philosophical basis for the objective of the New Economic World Order is the principle of distributive efficiency.

#### Finally a Projection

I have still not "projected" the New Economic World Order. I can only hope that the substitute will be considered more useful by serving future developments rather than present prophecies. What I would project if pressed to move up to the level of my incompetence is that there will be a continuing increase in helping the poor, with the benevolence continuing to be disguised as insurance and as conscience money for damage by monopolistic restrictions as in Arabian oil or American soy beans (and now in American wheat and shipping). It will be combined with political bidding for allies and for bases by the rival world powers, and this will force attention to the preferences of the governments of the poor countries rather than to the needs of their impoverished citizens.

However, as the understanding spreads of the basic efficiency principles, the existing trend of raising minimum levels of living relatively as well as absolutely, will continue in the rich countries, and will spread to a similar raising of relative as well as absolute economic levels, both of the poorer countries and of their poorer inhabitants.

In the longer run I see in the capitalist countries a continuing decrease in the volume of rents and surpluses--the "un-necessary incomes"--being appropriated and justified as necessary for



efficiency; and in the socialist countries a continuing increase in the volume of payments to workers and management recognized as necessary material incentives for industry and efficiency. As the spread of technological knowledge diminishes, the differences between the "capitalist" and the "socialist" economies, the economic basis for the ideological conflict will weaken. Communication between the countries will improve technically as well as politically, and the chances of world peace may increase. But now I am indeed projecting far beyond my level of incompetence and perhaps beyond everybody else's.

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