

agreement. It is obviously necessary, since these are the two largest emitters of GHGs. It may well be sufficient, since if these two giants can agree, the rest of the world will fall into line" (p. 209). In addition to this important conclusion, the main policy suggestions Llavador, Roemer, and Silvestre list at the end of the book can be summarized as follows: First, the climate change problem cannot be solved at the global level, unless international negotiators recognize the connection between restricting emissions and curbing growth. Second, investment in education should rise well beyond current levels and a larger fraction of resources should be allocated to the production of knowledge, which boosts technological progress. Third, the price of carbon should be substantially higher than what has been observed in recent permit markets.

The strong points of Llavador, Roemer, and Silvestre's book are to be found in the convincing arguments for developed and developing countries to better cooperate in the reduction of gas emissions, as well as to take these issues more seriously than it has been the case over the past decades. To discuss sustainability by considering a global point of view on economic activities, rather than at a national level, is an ambitious task. Nevertheless, the authors appear to have succeeded in this. They convincingly show the advantages of their approach to sustainability compared to other analyses in climate change economics, particularly those proposed by Robert Stern (2007) and William Nordhaus (2008, 2013). What is possibly missing in the book is any reference to or an argument against some more radical views like those on a degrowth society. Nevertheless, *Sustainability for a Warming Planet* is a must read for economists focusing on climate change and for any scholars interested in discussing new paths to sustainability, to limiting global warming, and to preventing its dramatic consequences for humanity.

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Book Review

The Heterodox Theory of Social Costs, by K. William Kapp, edited by Sebastian Berger. London: Routledge, 2016. Hardback: ISBN 978-1-13877-547-3, \$160.00, 166 pages.

The Foundations of Institutional Economics, by K. William Kapp, edited by Sebastian Berger and Rolf Steppacher. London: Routledge, 2011. Hardback: ISBN 978-0-41558-655-9, \$60.95, 286 pages.

The first book under review is dedicated to Fred Lee and contains thirteen chapters on social costs by the German-American economist (1910–1976) and author of *The Social Costs of Private Enterprise* (1950), K. William Kapp (who was also a founding member of AFEE). The unpublished and previously untranslated articles come from the Kapp archives, which were written between 1936 and 1974. In his excellent short introduction, Sebastian Berger (senior lecturer of economics at the University of the West of England and a trustee of the Kapp Foundation) points out that Kapp's approach still should serve as the basis for a heterodox theory of social costs. It could serve as a sturdy bridge between various heterodox paradigms with its substantive-holistic approach and criticism of the faulty logic of neoclassical (environmental) economics and its normative-apologetic character.

Every sentence of this book deserves reading and proves Kapp's originality, his broad knowledge of the social sciences (including philosophy and anthropology), and his concrete awareness and knowledge of contemporary trends in the economy, society, and environment. These abilities were interlinked with his power of judgement as a highly educated and morally motivated intellectual, who also anticipated early on long-run trends and dangers. It is not possible in this review to adequately highlight Kapp's fascinating writing and thinking beyond stereotypes and clichéd wording. Highlighting only certain aspects should suffice here. Kapp was an early critique of hyperglobalization. In the tradition of the doctrine of productive forces (List) he advocated protectionism to favor a balanced economy that combined agriculture, manufacture and commerce, even if this could be attainable only at the cost of lower living standards. "Universal free trade would only be possible and equally desirable for all under a system of world government which has eliminated the danger of war" (p. 63). Kapp cited Adam Smith's dictum that defense is much more important than opulence and that it was more important to sell to one's friend than

to an enemy – from a European perspective, we could add to totalitarian regimes like Saudi Arabia, Russia, or China which leads to a problematic international policy of accomplices (Syria). Parts of the texts were written during WWII, but there are many reasons to revitalize the idea of a more balanced economy (see the TTIP debate) that prevents social and ecological dumping.

With respect to international trade, (subsidized) transportation costs come into play and Kapp aptly criticized the inefficient “mixed” systems of transportation. This validates the recognition of special policy domains in an overall and holistic perspective. The definition of a formal general optimum was exposed as shallow, and Kapp pleaded for the pragmatic discussion of social priorities, critical ecological zones with regard to depletions, and the scientific agreement of social minima “in such fields as public health, medical care, education, housing, civilian defense, transportation, and recreation” (p. 103). Kapp’s thesis was that a substantive definition of social costs (and social benefits) only makes sense when these minima were defined and targeted in both developed and developing countries (for some time, Kapp stayed in India and the Philippines). I will mention one further peculiarity concerning methodology. According to Kapp’s evolutionary, open-systems approach, with constantly changing and evolving subsystems often with positive feedbacks and trigger points, he doubted “(as Myrdal also does) that we will ever be able to acquire the complete and quantitative information required to formulate an interconnected set of equations describing the movement and internal changes of the relationships within a social system” (p. 137). Kapp correctly questioned the modelling approach, which comes dressed in many different clothes today (including complexity modelling approaches).

“Institutional economics is much better known as a critique of conventional economic theory than as a system of analysis in its own right” (p. 14). The second book I review here, *The Foundations of Institutional Economics*, remedies this lacuna. Beginning it in 1960, Kapp never completed this book even though he worked on it for over sixteen years. He did complete ten chapters of it, comprising a total of 158 pages. The remainder of the volume contains other valuable articles, which fill some of the missing information from the unfinished topics and chapters. For example, Appendices F and G are excellent inserts on the differences between mainstream and critical institutional approaches, while Appendix H presents alternative introductions for *The Foundations of Institutional Economics*. The editorial introduction by Sebastian Berger and Rolf Steppacher (Steppacher is a graduate student of Kapp and a member of the Board of the Kapp Foundation), offers a short biography of Kapp, discusses Kapp’s attempts to establish an international institutionalist organization, and sums up the thirty-year fate of this unpublished manuscript which is part of the Kapp archives. I agree with the editors that the text is of great significance to heterodox economics, “with a primary interest in economic and cultural change under the combined impact of technology and investment for profit, a refusal to draw the boundaries of economic analysis in accordance with any normative notion of what is ‘economic’ and ‘non-economic,’ and a critical attitude towards the perceived hidden biases and preconceptions of pure economic theory” (p. 15). Kapp’s approach was

integrative and stressed the complex and circular interdependencies that link the various parts of the socio-economic process as an open complex system and its culture, which can hardly be understood in the confines of general equilibrium analyses. The latter also serves to justify and rationalize the status quo, assuming an autonomous sovereign consumer. “Once young economists have mastered the neoclassical language, concepts, definitions, and distinctions, and have become accustomed to the neoclassical mode of thinking, they will find it difficult, if not impossible, to escape its implicit normative conclusions” (p. 29).

The foundations of Kapp’s work are the ideas of Thorstein Veblen, who has been recognized as the most influential social scientist due to his elaboration of *homo institutionalis*. Additionally, the works of Gunnar Myrdal, John Dewey, John R. Commons, John M. Clark, Max Weber, Frederic List, Charles Sanders Peirce, John Stuart Mill, and Karl Marx (see ch.3 on intellectual precursors) were recognized as theoretical cornerstones. Kapp’s surveying was subtly nuanced, so he emphasized the institutional aspects in Adam Smith, as well as the mechanical similarities in Marx and neoclassical economics. The fourth and fifth chapters of the book, dealing with the nature and meaning of institutions and with human conduct and economic behavior, respectively, belong among the best works ever written in the critical institutional tradition. Having defined institutions broadly as habitual patterns of thought and action (Veblen), the book highlights the biological fact that humans are unfinished animals (Friedrich Nietzsche) without automatic and stable behavior-and-response patterns. Man’s malleability (Arnold Gehlen) necessitates selected and stabilizing habits and patterns and respective social character structures (Erich Fromm) to let human societies function. In addition to practical knowledge for survival and organizing collective action, institutions also generate symbolic meaning to human action and life. Kapp, therefore, did not integrate Clarence Ayres’s distinction between technological serviceability and ceremonial irrationality of institutions, as the editors accurately remark in the introduction.

Kapp’s bio-cultural interpretation of institutions as the focal starting point of social economic thinking in contrast, for example, to the narrow scarcity view (Lionel Robbins), does not diminish the conservative and repressive character of institutions – institutions that develop a certain degree of autonomy which often makes them dysfunctional and outdated. Institutions may also embody the destructive and predatory human propensities stressed by Veblen. Humans typically aspire for higher status and consumption levels that are beyond their reach. Emulation drives the lower and middle classes to want to identify with the upper classes and with certain hegemonic habits of thought (see the presidential candidates in the US). This pervasive, popular insistence on conformity reinforces the inertia of institutions. Kapp also exemplified the significance of the critical institutional approach of a relational consumption in contrast to Keynes and Milton Friedman’s hypotheses, for instance.

Kapp offered an encompassing theory of economy and society. Social minima follow naturally in the sixth chapter because the aforementioned emulation and relative status hypothesis imply a distinction between basic and relative status goods, and Kapp distinguished between conspicuous and non-conspicuous consumption. In

his view, justified existential human needs are pivotal. They can be based on empirically tested knowledge that helps to define criteria of minimum adequate living conditions. Instead of a purely material-goods maximizing perspective, he underlined the importance of self-affirmation, self-respect, and safety needs. It is not welfare, utility, or happiness that are of major political concern, but the prevention of material and interpersonal relational suffering. This does not mean that socio-economic policy should be based on vague humanitarian considerations, but on "vital, biological existential needs, such as those related to food, nutrition, water, and air; but other basic needs of an emotional or psychological character, such as self-esteem and security, are also inadequately satisfied in many affluent industrial civilizations" (p. 97). These satisficing levels must embrace the ecological danger points, and they have to "place the substantive problem of existence and survival at the center of economic analysis" (p. 97). Kapp discussed issues that had been newly rediscovered, such as the post-growth and happiness research and debate. What is more, numerous food and water poisoning scandals demonstrate that, amid a life of plenty, social minima are far from guaranteed.

With his call for a certain planning and direction of investments to put the social minima at the center of concern, he refreshingly deviated from some institutional contributions that underlined the adaptation to changing situations and directionless evolutionary change. Kapp, however, wanted to give socioeconomic evolution a volitional and conscious direction. In a paper from 1972, reproduced in Appendix A of the book on substantive and formal rationality (2011, pp. 159-169), he called for a clear ecological orientation and a preselection of alternative technologies, inputs, production sites, and rules of behavior for firms and individuals. This seems necessary to influence the cumulative total process in order to limit the exploitation of our planet. Technology should not be treated as having its own laws, but as a regulated quantity and a dependent variable. Basic human needs should be articulated and implemented in accordance with "alternative technology possibilities and their consequences by means of participative planning" (p. 235; see also Appendix B on circular and cumulative causation, Appendix C on social costs, Appendix D on why indirect measures in conformity with the market system will not work, and Appendix E on how science and technology should pragmatically be organized).

In the seventh chapter on capital and capital formation, Kapp demonstrated the lack of reality in the neoclassical theory of production and production functions in order to "stress such socio-cultural elements as socially transmitted and shared knowledge, skills, habits, attitudes, and above all such dynamic factors as science and technology" (p. 103). Capital contains tangible physical equipment and intangible human knowledge. Instead of formal definitions of capital (values) of single firms and their productivity, capital (formation) is analyzed in a broader institutional framework as the *common* stock of technological knowledge (exploited by Alphabet, Facebook, LinkedIn, and the likes). It includes intellectual capital, institutional arrangements, infrastructure, social capital, scientific knowledge, and others. To explain distribution, the strategic position of income, power, dominance, asymmetrical social influences, and manifold and complementary input-factor relationships together play a major

role. "[A]ll incomes, other than profits are regarded as agreed-upon deductions, not in a process of perfect competition, but rather in a process of haggling and cajoling. Profits are residual items, not remuneration for an entrepreneurial activity ... but rather due to strategic positions of large-scale incorporated production units to manage, develop, and engross the current technological efficiency of the community" (p. 109). Surplus should not be defined on a micro-level, but it is the difference between "the aggregate product and socially necessary costs of production ... The size of the surplus, and how it will actually be used, are above all a function of culturally conditioned behavior patterns, valuations, and attitudes, and also depend on the distribution of power and economic dominance of some groups or classes" (p. 116).

The next two chapters give attention to technology and business enterprise, and the way they interact. Kapp pointed out that the system of private property, competition, and investment for profit does not necessarily push investment and production in a socially serviceable direction. Based on Veblen, he distinguished industrial and pecuniary employments of resources to describe the potential conflict between technological possibilities and a profit business orientation. In a profit business orientation, actors try to generate profits by shifting costs to others, by curtailing the capacity of others, by accumulating market power based on consolidation and centralization, by entering tacit alliances and common agreements on prices, by advertising and creating prestige (goodwill), and by using outside stimuli provided from the state. Critical institutionalists like Kapp did not only criticize Say's classical thesis that supply creates its own demand, but they also did not take for granted the Keynesian positivistic identification of anything that is produced and finds a market with a rational allocation of resources. Methodologically, institutionalism "uses neither the arithmetical apparatus of macro-analysis, nor does it search for factors which influence national output and employment in a fixed and unique (and hence determinate) manner. This is why institutionalists are so skeptical that such an inherently cumulative process can ultimately be brought under control" (p. 142). In Kapp's view, all these activities to encourage the cumulative process of expansion, including the injection of additional purchasing power as well as public expenditures for war and defense, have the potential for inflation and irrational exuberance.

Furthermore, like Veblen, Kapp doubted that various measures to redistribute income (i.e., progressive taxation, higher wages, shorter working hours, etc.) would be able to compensate the surplus productivity of the machine industry because public policy is necessarily guided by business interests in generating a desired level of profit to induce investment. In the final chapter on economic domination and the multi-sector economy, Kapp described the mixed economy with few concentrated large-scale giant corporations, the public sector, and small and medium-scale enterprises (including Galbraith, Berle, Means, and Perroux). Only the latter sector corresponds to the image of competitive markets, according to Kapp, whereas the overall economy is dominated by the coercive guidance of big business and administered prices due to their bargaining strength.

Mainstream economics today is not narrowly restricted in a mechanistic equilibrium approach (but it is still prevalent in many textbooks). Today, many topics that Kapp raised in his integrated approach are included in the happiness research, as well as in ecological and behavioral economics. Nevertheless, Kapp's *Foundations of Institutional Economics* still suffers from the main methodological shortcomings of mainstream economics: namely, the modelling approach and econometric testing (Colander 2000). Kapp doubted "that we possess or will ever possess the data and the type of mathematics needed for the quantitative formulation of mutual circular interdependencies, and thus for a precise expression of coefficients of interaction ... Social science ... as an instrument of prediction must stay at an intermediate level of analysis between the ideographic approach of many historians and the level of abstraction at which pure theory or mathematics prefer to proceed. Causes and effects in social systems interweave in a concatenation of reciprocal and cumulative interaction" (pp. 175 and 250; see also p. 268). Similar to Charles Wright Mills, Kapp accentuated the institutionalist quest for data, facts, and quantifications where it makes sense (see, for example, Mitchell's work on business cycles [1927]), but instead of overdrawn mathematics, the integration of materials and perspectives from other disciplines are necessary.

On a substantive level, it is of utmost theoretical importance today to observe the relevance of recurrent financial crises and the remedies of the "predatory state" both in the US and Europe. Although it was never completed (especially in regards to concrete reforms needed, which remains the task of today's institutional economists), *The Foundations of Institutional Economics* offers a valuable, readable, and profound introduction to critical institutionalism. This book should be read by all students of economics as it serves as an antidote to the economic mainstream and pushes against conventional indoctrination.

However, the book is more than that. It presents a holistic view of critical institutionalism with a positive, but realistic image of man as a creature of self-contaminating instincts, wasteful emulation, and conservative cultural leanings. The book also offers a critique of the biological foundations of institutions and their ambiguities – a still valid critique of the mainstream, and presents a social target function (social minima), and methodological devices (cumulative causation). It presents a holistic concept of capital and accumulation, a social value theory, a relational domination approach for the basic economic structure (multi-sector economy), and a quest for the respect of ecological survival constraints in due form of an *ex ante* process of democratic planning. It must be embedded in a necessary cultural revolution to change our ingrained common habits of thought. In Germany, Kapp's call for a critical renaissance of economics was recently reflected in the foundation of the private Cusanus University (www.cusanus-hochschule.de) and in the introduction of a pluralist master at the University of Siegen (www.master-plurale-oekonomik.de). Let us hope that a thousand flowers of critical heterodoxy will now blossom.

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