Review
Reviewed Work(s): A Capitalism for the People: Recapturing the Lost Genius of American Prosperity by Luigi Zingales
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Source: Journal of Economic Literature, Vol. 51, No. 1 (MARCH 2013), pp. 211-214
Published by: American Economic Association
Stable URL: http://www.jstor.org/stable/23644721
Accessed: 01-08-2017 19:50 UTC

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admitted by the author, it is not clear whether the GIF framework works for middle income developing countries. He cites Korea as a positive example but the story is not generalizable. Fifth, the need for a committed and capable government if corruption is to be avoided is given scant attention. Finally, and of some consequence, the relationship between the still predominant agricultural sector and industry in a dual economy setting is virtually ignored.

But, on the whole, this is indeed a stimulating volume, clearly indicating the author's extraordinary command of the development literature and his equally extraordinary level of motivation in making his case.

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The title of A Capitalism for the People by Luigi Zingales suggests a play on Abraham Lincoln's Gettysburg Address in which he describes for the American nation "a new birth of freedom—and that government of the people, by the people, for the people, shall not perish from the earth."

Zingales worries that the United States is at risk of becoming a nation of a government for the cronies, the special interest groups, and the big business people, not to forget some pork-barrels thrown in for the politicians. Both Democrats and Republicans have been engaged in these kinds of activities to win votes, get more campaign funding from the business community and increase the chances of wonderful job offers in the private sector when they leave office.

A Capitalism for the People is nonpartisan in a subtle way. It calls for small government in the sense of limited and simple interventions that can be understood by the people—who can oppose them if they are not for the people. The growing complexity of regulation has opened the doors to manipulation. The book also calls for small business in the sense of making markets more competitive and not letting firms get so big that they start to influence government. This influence is the main cost of big business and has been especially problematic in the finance industry.

Within this understanding of the problem, the Tea Party has a point: government is not properly governing for the people. And Occupy Wall Street has a point: big business is enriching itself at the people's expense. The book's powerful pop-competition message is aimed at reconciling both sides of the partisan divide.

What would Abraham Lincoln have made of it? In words long remembered, the President reminded his audience that America had been "conceived in Liberty, and dedicated to the proposition that all men are created equal." Zingales believes that U.S. capitalism is at risk of denying these origins; that some men and women in America have become too unequal in terms of economic opportunities. What is needed is more competition to unleash everyone's chances of benefiting from markets.

The first half of the book is a wide-ranging discussion about how the American Dream of equal opportunity is at risk. The government appears not to be properly governing for the public interest. Examples are given that may support many economists' views that regulations are often chosen to help big business people, or politicians, or both, along the lines suggested by public choice theory. Zingales discusses how Adam Smith's (1776) Wealth of Nations extolled the virtues of competition and the threats against it coming from the capture of government by big business. Alternatively, politicians may seek to lessen competition to enable more rents from which they can extract bribes.

However public choice theory also appears unable to fully explain the history of regulation. Post-1980s there was significant deregulation in many countries, especially in the banking and finance industry. To this day, the banking and finance industry in the United States and United Kingdom supports less regulation. The regulatory instincts of the European Union in Brussels horrifies the City in London. Could politicians and bankers be scheming to deregulate in their own self-interests?

To help answer this question, Zingales discusses how deregulation led to bigger banks that could
take advantage of their size to operate more efficiently. But their bigger size also gave them more political influence and their interconnections created systemic risks. Lurking underneath were “too-big-to-fail” implicit government guarantees. The book also suggests that financial products in an unregulated market are sometimes deliberately designed to be too complex for the people to understand. We may suffer from overoptimism in our ability to repay loans on time and fall victim to “teaser” offers. Sophisticated banks may be able to exploit people’s mental and behavioral limitations in the absence of any rules.

Another view is that there was a great deal of popular support for the deregulation and income tax cuts that were begun in many countries in the 1980s. Back then, capitalism had earned a high degree of legitimacy and the public mostly supported politicians offering less intervention. Maybe the fall of the Berlin Wall at this time also heightened beliefs that capitalism had won the day and was good, whereas the alternative system, communism, had lost and was bad.

However, the legitimacy of capitalism has been undermined in more recent times. In the long-run, free-markets cannot survive without the support of us, the people. Should we lose faith in the capitalist system, Zingales discusses how people may decide to opt out. Why bother trying to compete when capitalism is rigged against you? People may also vote in a new political movement that supports high regulation and high taxes out of anger against the establishment. The system may then risk being destroyed altogether in a fury of populist punishment and retribution.

In other words, high levels of intervention may be imposed in this kind of environment though not for any reason to do with the desires of big business people trying to protect themselves by working in cahoots with politicians. This amounts to a new theory of regulation. And it may help explain how the baby of capitalism could be thrown out with the bath water.

To avert this scenario, Zingales strives to uncover what factors are causing people to increasingly distrust capitalism. Subsidies, bailouts, and public–private partnerships whereby the best connected are supported are the focus of his blame. The political influence of big business and lobbyists are other culprits. Corruption and unethical behavior play a major role. Zingales puts these activities at the center of his rallying cry against “crony capitalism.”

The book quotes evidence from surveys of people’s support for capitalism to back up its views. Once we know what is causing people to turn their backs on capitalism, it gives us guidance about how to restore faith in the system. Only by stamping out cronyism will people believe in a just world whereby success is more determined by hard work or ability, rather than by luck or knowing the right people. Higher ethical standards in business may also be needed to stop the impression that the public are being exploited, if given half a legal chance.

This way of thinking is a novel behavioral, or psychological, approach to explaining macroeconomics. It describes a world in which the emotions—public disgust about a CEO’s whale-sized remuneration when his bank is going bust—or anger when a company is bailed out even when it is badly managed—can start explaining future growth rates.

By withdrawing effort when emotionally offended about the system being unfair—or by voting for political parties that promote punishment of bad business people through regulation and higher taxes for everyone—we, the people, can start making economic prosperity disappear. We may be inclined to act these ways even at a material cost to ourselves, in a similar way to how people reject unfair offers in the ultimatum game.

The second half of the book is about how to change the way that capitalism is operating in the United States to regain people’s trust and return the competitive free-market ideal back into a powerful populist movement. It’s a great read since most of the proposals that Zingales describes are not found in conventional textbooks and invite us to rethink traditional approaches to public policy.

Before he outlines policy solutions, Zingales sets the scene by describing how technological progress, globalization, and corporate avarice these past decades have given way to a “winner-takes-all” society in which the middle classes have been squeezed. Together with the burgeoning costs of higher education and health-care in the United States, a bleak picture is painted in which many people have little hope of being winners. To add insult to injury, rising levels of cronyism
in politics have been piled on top of these other problems.

Zingales calls for antitrust legislation to be reinvented to reflect the costs of the political influence created when big business gets bigger and has greater power to manipulate regulations in its favor. A narrow consideration of the direct economic costs and benefits of scale misses the point.

A Capitalism for the People also stresses the need for markets to be underpinned by ethics and trust in order to prosper. Kenneth Arrow (1973) once observed how economists frequently take the self-interest, profit maximizing assumptions made in their models the wrong way by asserting “that firms ought to maximize profits; not merely do they like to do so but there is practically a social obligation to do so” (303).

Zingales discusses how ethics and trust may help solve market failures in more efficient ways than regulation. He regards “civic capital” as being particularly important. But how can the sort of behavior that helps markets prosper be encouraged? A firm may not have an incentive to enforce good ethical codes when its profits are put at risk. Even worse, bad behavior by one firm may have negative externalities on other firms by lessening people’s support for capitalism as a whole.

The author believes that business schools should not be afraid to teach prospective managers how they ought to behave so as to be “good capitalists.” The wider purpose is to make responsible behavior a social norm so that the public become more supportive of capitalism as a whole.

Zingales would also like “lobbying” for influence to become a dirty word and a social norm established that makes it sound like “smoking.” The amount spent on lobbying should be made public and the damage inflicted by lobbyists exposed. The book dismisses trying to regulate lobbyists since regulating the very people who are experts at capturing regulation would be inviting trouble. The best solution would be passing a zero-tolerance law aimed at eliminating all subsidies to industry so that the lobbying beast cannot be fed.

More generally, A Capitalism for the People urges regulation to be limited and simple to understand, preferably enforced by a whistleblower reward system. The inefficiency of too much simplicity may be far less than the inefficiency arising from complexity deliberately created by lobbyists to create loopholes. Another option is to use Pigouvian taxes to replace regulations. Taxes can help correct distorted incentives but are less vulnerable to capture by vested interests.

Regulation that is understood by none of the people, influenced by the lobbyists, for their clients, is something that Abraham Lincoln may have wanted to perish from the earth. It alienates us from “the system.”

The book also calls for reform of public education in the United States, which it blames a great deal for killing the American Dream for lower income groups. Zingales believes that education should be state-funded but not state-provided. He suggests that a voucher system would improve teaching quality. People from less privileged conditions could be given higher value vouchers and schools could be incentivized to rescue disadvantaged students. Reforming the public education system along these lines would be one of the most important ways to create equal opportunities for all Americans while maintaining competitive incentives through nonequal outcomes.

There is one issue that should be put in context about A Capitalism for the People. The author has a deep faith in markets and wishes us to return to more pure forms of competition. He views the reaction against capitalism, especially since the “Great Recession” of 2008, as being largely due to big business and big government interventions that have lessened the ability of markets to deliver prosperity for all the people. However there is another view.

One of the recognized primary causes of the Great Recession was the collapse of the house price bubble in the United States. Zingales suggests that it should have been pretty easy to spot although acknowledges that Robert Shiller was about the only one of us who did. Perhaps people are doubting capitalism since they associate it with volatile markets whose prices bear little relation to the fundamentals. Maybe there is a growing belief that making money is about riding a bubble and getting lucky by selling out before it bursts.

In other words, is “cronyism” the cause of our problems or is the problem that competitive markets themselves are inherently unstable? Is eliminating the dark forces that have got in the way of competition the solution or should we instead shine more light on things like hedge...
funds that thrive on the roller coaster ride of free-markets and maybe exacerbate their swings? Of course Keynes back in 1934 pondered this kind of problem and asked whether markets should be made more expensive to access in a similar way to how gambling in casinos is often restricted.

Zingales provides a powerful piece of evidence against this view. It should make politicians and big business sit up and take notice. A majority of people surveyed in the United States believe that “The free market system is the best system to generate wealth.” By contrast, a majority believe that “Big business distorts the functioning of markets for its own advantage.” Public trust in government is also low. In other words, surveys suggest that people have not given up on markets, at least in America. But they are giving up on big business and big government.

Every economist should read A Capitalism for the People and ask their students to read it also. Since there is zero appeal to our consciences in most standard economics textbooks these days, Zingales’s book is a great complement. Understanding how our emotions, beliefs, and limited understanding of complexity can influence whether capitalism flourishes or fails is just beginning. Few economists have tried to reinvent how to govern for the people in the context of the behavioral realities of the people. This great book by one of the people, Luigi Zingales, may be an important leap in the right direction.

References

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JEL 2012–1543

The last two decades of controversy over agricultural biotechnology across the world have inspired an enormous amount of social scientific scholarship across multiple disciplines. Much of this work has focused on understanding the opposition to this technology and the dramatically different approaches to governing it, particularly in the United States and Europe. Seeds, Science, and Struggle seeks to contribute an additional sociological perspective to this body of research. Focused on these politics in Canada and Mexico but with a broad eye toward the nature of these controversies across the globe, Kinchy explores the strategic choices of the activists who have challenged these technologies, and makes two main arguments that may be of interest to the economics community. First, despite the interpretation of many proponents of agricultural biotechnology, activism against this technology is not borne simply out of scientific misunderstanding. The savviness of these activists is clear from the way they engage with science. While they are often quite critical of the scientific enterprise and science’s privileged status in guiding and justifying public policy, arguing that it tends to focus on quantifiable questions about cost and safety rather than broader concerns about social justice, they also realize that they must contend with it in order to create meaningful change. So, like the multitudes of critics who have emerged to challenge modern science and technology over the last forty years, anti-biotech activists cannot avoid fighting their battles at least partially on the terrain of science itself. This, of course, puts them automatically at a disadvantage, as they generally lack access to the resources, experts, and corridors of power that benefit the scientists and companies who promote agricultural biotechnology. It also requires creative strategic choices, as they simultaneously use science to justify their positions while also challenging its foundational role in policy making.

Second, Kinchy notes that these activists are not merely acting out of their economic interests. Rather, they are at least as focused on advancing an alternative worldview that provides greater deference to tradition and culture, and replaces dominant institutions and power structures with those that seem more democratic and equitable.