The Design of Free-Market Economies in a Post-Neoclassical World

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ABSTRACT: The Design of Free-Market Economies in a Post-Neoclassical World

The ‘Washington Consensus’ supporting competitive frames and market solutions in economics and law was shown inadequate to address social problems in non-U.S. settings. So would diversity and dynamics suggest theories in need of adjustment to other realities such as culture, increasing returns and market power. Reform must account for an economics of falling cost, ecological limits and complementarity in our relations. Such shall open new applications for economics and law.

In this paper a theory of planning horizons is introduced and then employed to raise some meaningful questions about the neoclassical view with respect to its substitution, decreasing returns and independence assumptions. Suppositions of complementarity, increasing returns and interdependence suggest that competition is inefficient by upholding a myopic culture resistant to learning. Growth – though long believed to rise from markets and competitive values – may not derive from these sources. Instead, as civilizations advance, shifting from material wants to higher-order intangible output, they evolve from market tradeoffs (substitution and scarcity) into realms of common need (complementarity and abundance). If so, then neoclassical arguments shall no longer apply to any advanced information economy also restrained by its ecology.

Indeed, this paper opens standard theory into a more general framework constructing ‘horizon effects’ into a case for cooperation – as more efficient than competition for all long-term problems of growth. The case is made that competition is keeping us stupid and immature, rewarding a myopic culture at the expense of learning and trust, therefore retarding economic growth instead of encouraging it as believed.

The policy implications of horizonal theory are explored, with respect to regulatory aims and economic concerns. Such an approach emphasizes strict constraints against entry barriers, ecological harm, market power abuse and ethical lapses. Social cohesion – not competition – is sought as a means to extend horizons and thereby increase efficiency, equity and ecological health. The overriding importance of horizon effects for regulatory assessment dominates other orthodox standards in economics and law. In sum, much of the reason for the failure of the Washington Consensus stems from myopic concerns central to any horizonal view. Reframing economics along horizonal lines suggests some meaningful insight to how regulations should be designed to keep pace with this approach in economics and law.
KEYWORDS

growth, complementarity, planning horizons, social welfare
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1. Introduction

The ‘Washington Consensus’ – as the term is currently used (Williamson 2000) – describes an ideological view which places privatization and competition at the top of the social agenda for economic development. This paper raises some basic questions about the virtues of competition, deriving from its suppositions about human relations. Social theory in economics starts with individual wants, independently framed and achieved. Furthermore, rivalry is endemic: competition is the best means to reconcile opposing intentions, shaking out those who want things most in a process of financial gain. The whole story is founded on neoclassical theory and its view of competition as efficient in the general case. Neoclassical economics is centrally based on substitution as the defining characteristic of economic relations. Substitution, in turn, derives from production under rising cost (diminishing returns). Substitution also warrants independence assumptions (Krupp 1982, p. 390; Jennings 2007d) and the use of equilibrium models.

The whole scheme unravels with these suppositions relaxed, to favor complementarity, increasing returns and interdependence. In this setting, there are no equilibria and the economy opens along a path-dependent track where ethics and history count. The virtues of freedom and efficiency – individualism in general – ought to be addressed differently in a post-neoclassical world; their ramifications suggest that collaboration – not competition – may be a better route to economic growth in a more realistic context. The aim of this paper is to explore the optimality of free-market economies under revised assumptions, and the social policy implications of this shift away from mainstream models of choice.

The basic characteristic of the alternative frame proposed is an embrace of complex interdependence – substitution and complementarity inextricably intertwined – in an economic context of increasing returns to new output. Under this supposition, justified by A.C. Pigou (1927, 1928) and reinforced by Nicholas Kaldor (1972, 1975), production cannot encounter rising marginal costs save for short-term models subject to fixed inputs and other dynamic constraints. The underlying technology is of falling cost throughout the economy. Indeed, the case for rising cost stands on nothing more than assertion (Jennings 2007a, 2007c) due to the analytical limits of neoclassical theory.

Opening economics into realms of nonconvexity – as increasing returns will do – alters many established ‘truths.’ Substitution and decreasing returns allow equilibrium models to close, satisfying existence proofs for scientific acceptance. So would economic ‘convenience’ set the terms for legitimate discourse at the cost of realism. Complementarity and increasing returns are the way of our world; this paper aims to show why and trace some meaningful lessons therefrom. The paper is structured as follows. First, the joint importance of substitution and complementarity in economic relations is addressed to show why substitution is only one side of a two-sided coin where concerts and conflicts of value coexist throughout economic phenomena. Next, the twin notions of planning horizons and interhorizonal complementarity untangle an institutional quandary in which cooperation – not competition – is shown as efficient. The third section to follow will limn the growth and policy implications of a horizonal economics of complex systems and rational limits, suggesting a post-neoclassical view of free-market economies shaped by ethical laws, social culture and other considerations so far ignored in neoclassical theory. The last part of the paper restates its central conclusions and implications for economic growth and development in a world defined by ecological limits, rational bounds, common aims and horizon effects. So would doctrine need to evolve from competition to an inclusive frame adopting cooperation as our route to growth and development through an expansion of planning horizons in a new economics of information and organizational learning.

2. The Nature of Economic Relations

Substitution assumptions stand on notions of opposition as the basic characteristic of economic interdependence: social relations are rivalrous, since scarcity is the problem motivating individual effort to meet human needs. Substitution and tradeoffs state the nature of our relations; such is the way of physical goods, which either belong to you or another.
The conflicts of value assumed in this setting – associated with things as the source of economic well-being – create a rivalrous social linkage as a means to serve common needs. So would Smith’s (1776, p. 423) “invisible hand” deliver an optimal level of satisfaction to the public through free trade in a market society. Although some problems are acknowledged with this central lesson, it remains a prime motivation for the economics of growth and development. There has always been an underlying tension in economics, however, among immaterial outputs and those of physical goods. As Romer (1994, p. 204) expressed it, two types of input – things and ideas, or atoms and bits – serve to explain growth: the ‘nonrivalry’ of immaterial goods is seen to be important to the development process.

But Romer doesn’t go far enough in assuming constant and decreasing returns to scale in things: substitution is not the only form of interdependence, even in realms of physical output. The implications of falling cost – that transformed economics during the 1930s debates – suggest diminishing returns are not the long-term nature of production technology, even as noted by Adam Smith in his pin factory illustration of virtuous specialization (Warsh 2006, p. 46). Pigou (1927, pp. 193-97; 1928, pp. 252-56) ruled diminishing returns “impossible,” to be “excluded completely”: “only the laws of constant or decreasing supply price … are admissible.” Kaldor (1972; 1975, p. 348) endorsed increasing returns as the general case in production, yielding complementarity in our relations: “The principle of subdivision … ignores the essential complementarity between … different types of activities … which is far more important for an understanding … of the economy than the substitution aspect.” Myrdal (1978, pp. 772-74) outlined a similar view of “cumulative causation.” If true, then economics should embrace substitution and complementarity in a nondecomposable mix. Standard theory in economics seized on one form of interdependence at the expense of another, which may be “far more important…”

The relation of value to scarcity is also at issue here. In traditional economics, scarcity enhances worth, as with the water-diamond paradox: water is free though needed for life when useless jewels are rare and costly. A scarcity economics sees no problem with this scenario, whereas information network economies suggest a blindspot in this approach. As Matthew (2001, p. 2) reported in an essay on “The New Economy”:

> In the networked economy, the more plentiful things become, the more valuable they become. …Value is derived from plenitude, the concept of abundance. … Abundance is everything. Ubiquity drives increasing returns in a networked world. In fact, the only factor becoming scarce in a world of abundance is human attention.

This is the fundamental difference of complementarity and substitution, of falling and rising cost technology: the entire relation of value to scarcity vs. abundance shifts. Due to the reproduction of information “at near-to-zero marginal costs,” as Elsner (2004, p. 1032-33) explained: “The ‘new’ economy, thus, has entered a stage of informational abundance which bears little resemblance to the conventional mainstream economic assumption of scarcity.” Quoting Lamberton (2001, pp. 115, 117f), Elsner continued:

> “The limitations of information as a commodity…” call for a “thoroughgoing innovation in organizational design” to include “a very high level of collaboration.” This renders economics a science of (…) adequate coordination mechanisms rather than a science of individual maximization, general equilibrium and ‘optimality.’

An economics of complementarity opens some meaningful questions about traditional models of thought. If we step back from profit and pricing to look at human desires, why on earth would economists ever assume our social needs are opposed? Don’t we applaud each others’ success, as I might rejoice in yours? Is not the purpose of organization to align economic incentives into a more harmonious process (Jennings 2007e)? Are not emotions contagious in their interpersonal impact? Why aren’t we helping each other succeed, instead of competing here? All these spreading influences show complemenary interdependence.

Social conscience and personal growth internalize ‘externalities’ into the planning ahead of all choice. Substitution is not the only economic connection, nor is competition always efficient: in the presence of complementarity, cooperation is sought. Embracing complementarity opens economics in new ways: equilibrium may not occur in a positive-feedback
system with a path-dependent historical lineage. Complex interdependence – substitution and complementarity – undermines acquisitive values, showing cooperation may be preferred. The notion of planning horizons offers a way to resolve the dilemma.

3. **The Institutional Economics of Planning Horizons and Complementarity**

The economics of substitution and tradeoffs – ‘scarcity economics’ – stands on equilibrium models, where independence is the rule and externalities are the exception. In any event, spillovers shall attenuate as they spread, unlike ‘cumulative causation’ where external effects expand (Jennings 2007d). The economics of complementarity amplifies social links, so externalities stay uncontained. Unbounded interdependence, however, imposes some meaningful limits on our range of anticipation: this is how planning horizons serve as an index of bounded rationality. A network connection of pricing effects so will extend through planning horizons into a case for complementarity. The argument goes as follows: first, the individual pricing decision is examined; then its horizontal aspects are explored and applied in network contexts. Subsequently, a vital link between our planning horizons suggests contagious social horizon effects called ‘interhorizonal complementarity.’ After that, the post-neoclassical growth implications of planning horizons shall be considered.

3.a. **The Individual Pricing Decision.** Decisions are not made on known outcomes but rather among imagined projections of outcomes based on theory. ‘If I do this, then that will occur’ expresses a causal belief about the world derived from models selectively based on their own ‘essentials.’ Such essentials are only asserted: theory acceptance shows in use. Selective focus is also restrictively blind to what is ignored: theory is silent on its omissions. All amounts to a case for openness, multiple models and pluralism (Jennings 2007b); we cannot see what we miss or even imagine what we ignore. An act of choice is a normative process of multidimensional causal projection; these selective visions show a range based on knowledge, experience, self-awareness and clarity in our assumptions and applications. So will our expectations suggest a linkage of prices to planning horizons in need of formalization.

A static conception of pricing can be inferred through induction thus: a price is set, fixing output at one point on the market demand curve (functionally positioned through advertising, product design, etc.) over a unit cost determined by estimating the marginal value of inputs adjusted for risk. The opportunity cost of that price ($P^*$) incorporates all the expected profit streams of foregone prices on a demand curve framed by the agent, trying to fit her anticipations to the reality as it unfolds. The range of projection involved defines the planning horizon in choice; every pricing decision has a horizontal length as well: long-run curves in economics are more elastic than shorter-run curves. Such is the focus of any horizonal explanation of price.

The static conception of pricing in traditional theory is deduced from first-order conditions of profit maximization thus: $P^* = M^* \cdot E^*$ where $M^* \equiv MR = MC > 0$ is a measure of unit cost combined with a markup term $E^* \equiv \frac{\varepsilon^*}{(\varepsilon^*+1)} > 1$ based on its own-demand elasticity $\varepsilon^* \equiv \frac{dlnQ}{dlnP} < -1$. The main conceptual change involves epistemological status: $P^*$ rises out of inductive inference from an observed reality, based on uncertain expectation. In other words, the pricing decision depends on belief and assertion, not on knowledge and definite truth; the explanation entails a horizontal range in its suppositions. So will the run length of cost and demand curves – often derived deductively – be inductively inferred from price-setters’ planning horizons. The relation of price to planning horizons can be stated thus: $dP^*/dH^* < 0$ with $d^2 P^*/dH^*2 > 0$.

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1 Herbert Simon (1981, p. 103) remarked on neoclassical avoidance of subjective factors in economic analysis thus (also cf. note 13): There is a certain arbitrariness in drawing the boundary between inner and outer environments of artificial systems. …We might well have considered the business firm’s cost function to be part of the inner environment. Instead we abstracted the decision-making process from the production technology and regarded only the limits on rational calculation as inner constraints on adaptivity. The cost function was treated, along with the demand function, as part of the outer environment to which the firm was seeking to adapt.

2 This finding can be derived – if done properly – from Alchian’s (1959) nine propositions on cost, despite the erroneous effort by Hirshleifer (1962) and its acceptance by Oi (1967) and Alchian (1968): cf. Jennings (1985, ch. 5). Formally, $M^* \equiv MR = MC$ at $Q^*$ (the maximum profit condition), with $E^* = \frac{\varepsilon^*}{(\varepsilon^*+1)}$ where $E^*<1$ because $\varepsilon < -1$ (and here $\varepsilon = \frac{dlnQ}{dlnP} = \frac{dQ}{Q}/\frac{dP}{P}$), the
As Matthew (2001, p. 2) said, “the only factor becoming scarce in a world of abundance is human attention.” Indeed, a planning horizon (H*) exists in every act. Though H* is not observable, our projections have a range for each contingent track considered in a balancing of attention among competing demands. Attention is selective, so our choice of essentials counts: if frames don’t fit to applications (due to rigid assumptions), then our planning horizons shorten relative to what they might have been. The case for realistic conceptions shows in horizon effects, stemming from inappropriate theories. This paper reports an example in neoclassical claims.

Planning horizons serve as an aid to thinking about decisions and foresight. But H* is ordinal; ‘wits’ are innumerable, like ‘utils’ (Boulding 1966, pp. 22-23). So we speak of horizon effects as changes in planning horizons, without exact calibration of axes. The relation of P* to H* is seen in the following way: the longer the planning horizon – due to internal factors (such as self-confidence, knowledge, effort and energy) and to external factors (such as stability of the decision environment, trust in others’ reliability, and a lack of surprise) – the lower will be the marginal cost (M* > 0), the markup (E* > 1) and the price, where P* = M* • E* applies to all market forms. Perhaps Margolis (1960, pp. 531-32) said it the best; his statement is one in a long debate about time in relation to cost:3

... The greater the uncertainty ... the shorter ... the planning horizon and the greater ... the ... costs... The implications ... are that the greater the ignorance of the market the higher ... the estimate of the costs and the more inelastic the estimate of demand. What price should a firm charge if it has hopes of ... expanding its market? The higher the price the greater the expected short-run profits and the greater the sacrifice of expected information about the mass market. The lower the price the more information it gains about the future market possibilities.

A useful way to intuit the relation of planning horizons to price is that the planning horizon in choice is like the ‘move horizon’ in chess (Jennings 2007f).4 Standard assumptions – of free agents, known outcomes, stable wants – do not apply in chess. One must abstract from positions to address the problem of chess (or of oligopoly too). Chess is a process of planning in the face of strategic contingencies shifting with each turn. Outcomes are projected uncertainly, and the purpose – to win – neither restricts nor requires actions sufficiently to identify moves. The field of chess is as

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3 Knight (1921, esp. pp. 186-87) described the problem in his opening sentence with clarity:

Great difficulties are met with in stating a clear and straightforward exposition of price theory because of the fact that the given conditions or data of the problem are so different according to the length of the time period which the explanation takes into account. ... The essential fact in economics is that different changes take place at different rates, that for certain time periods certain aspects of the situation may be assumed to remain unchanged, while for longer periods some of these will undergo change. The data or given conditions are different when different periods of time are under consideration, ...

A helpful discussion of Marshall’s views in this regard can be found in Shackle (1965, ch. 3, pp. 27-42); also cf. Frisch (1950). Stigler (1939, esp. pp. 306, 311-12, and 320-21) closed his paper in a manner revealing the problem as methodological:

... a complete presentation (for any given set of price anticipations) involves a third axis, time, and the marginal and other cost functions become surfaces. ... But ... it is no longer possible to handle the problem ... by the use of plane geometry, since future prices are now important variables.

J. M. Clark (1940, esp. pp. 246-48) said “the whole functional relationship is probably so complex as to defy mathematical plotting.” Then Clark (1955, esp. p. 459) noted that:

This complex of variables would overload any possible system of graphic presentation. A family of three-dimensional surfaces – the third dimension being time – with a different surface for each initial price or price situation, would still be a simplification.

Also cf. Turvey (1969, esp. pp. 285-87), who concluded on p. 287 that:

... The definition of marginal cost as the first derivative of cost with regard to output is too simple to be useful. Both cost and output have time dimensions, and both may be subject to uncertainty.

4 Waldrop (1992, pp. 150-51) quotes Brian Arthur’s response to “What is the real problem with economics?” as “Chess!”
much an opponent’s style of play as the board. The chessboard demands a different approach to understanding choice than neoclassical theory allows.

The better that tradeoffs are understood and near-move contingencies culled, the more moves ahead can a player project. The emphasis here is on planning in unpredictable changing conditions. Choices in chess are path-dependent, spatially interdependent and irreversible, as in real life. One must step back from pieces on the chessboard to its economics: the move horizon in chess is analogous to the time horizon in choice. But time horizons are only extended by knowledge of other relations, so planning horizons remain the focus. Planning horizons serve as an ordinal index of ‘savvy’ in practical life, framing the ‘appropriateness’ of our applications.

Formally, one can think of these static constructions (setting P* as the product of M* and E*) as members of a horizontal family. Cost and demand curves shift with horizon effects in predictable ways, since longer-run curves, ceteris paribus, are more elastic (or flatter) than shorter-run curves. If each static graph is on a transparency in a horizonal file drawer (with longer horizons toward the back), the horizontal part of Figure One is a side view of that file tracking P* and M* for different H*s (while leaving Q* implicit). See Figure One below.

3.b. The Interrelations of Pricing Decisions. But Figure One only describes single price-setting agents, with no account of externalities (pecuniary or otherwise). In neoclassical theory, aggregation from individual prices to group patterns is set by industries, which impose substitution by fiat. This is fine for beer vs. wine in the context of having a drink, but fails for wine, beer, cheese and pretzels when the choice is to party or not.5 A transportation network captures the problem in a more flexible way; that is where Chamberlin’s work on monopolistic competition began (Chamberlin 1961).6

5 In this case all of these products are complementary, competing with non-party options.
6 Cf. Jennings (1985, 2006). Friedman (1953, pp. 38-39), as quoted in Jennings (1968, pp. 21-21), rejected Chamberlin’s framework on the grounds of the impossibility of relaxing the industry designation:

... It would be highly desirable to have a more general theory than Marshall’s, one that would cover at the same time both those cases in which differentiation of product or fewness of numbers makes an essential difference and those in which it does not... The theory of imperfect or monopolistic competition developed by Chamberlin and Robinson is an attempt to construct such a more general theory...
In this setting, concern should focus on externality issues, on the impact of any particular price on the profits of other price-setters, either *ceteris paribus* for their prices or *mutatis mutandis*. Either way, net interdependence within any group with respect to \( P_j \) is the difference between an uncompensated \( P_j^* \) and a \( P_j' \) including external profit effects. The impact of \( P_j \) on any firm \( i \neq j \)'s profit is simply \( s_{ij} = (Q_{ij}/Q_i) \cdot (M_{ij}^* - P_{ij}^*) \cdot [\varepsilon_{ij}^*/(\varepsilon_{ij}^* + 1)] \), so net effects are a combinatorial \( S_i = \sum s_{ij} \).\(^7\) Consequently, \( P_j' = P_j^* + S_i \); if \( S_i > 0 \) then we have net substitution within this group with respect to price \( P_i \); this is much like an industry model. But with \( S_i < 0 \), we have net complementarity. The interdependence within any group with respect to a single member can thus be expressed in general terms unrestricted by industry aggregation.\(^8\)

But now, with blinders of substitution (negative feedback) cast aside, we have an institutional problem. With substitution, competition will lead to greater output: that is the orthodox story. Yet among complementarities, it is collusion augmenting output and growth, where *rivalry yields scarcity*. Any institutional system, be it competitive or cooperative, enhances substitutes – starving complements – or just the reverse. This is why intangibles suffer in adversarial systems. Sadly, we must choose, at the (invisible) cost of foregone options.

Rivalrous social incentives stifle complementary output. A nondecomposably intertwined tangle of substitutes and complements sets up a problem of policy choice: which is more important, substitution or complementarity? Do we know? Have we studied the question? Can we design our institutions for competition across substitutes and collusion among complements, when that distinction is so preference- and purpose-specific? Is there a way around this problem of interdependent typologies?

In the formal analysis of a transportation network context, the term \( S_i \) expresses the balance of substitution and complementarity in any group with respect to one member. The question to ask concerns the impact of a *horizon effect*.
– for longer or shorter, wider or narrower, better or worse – on that balance \( S_I \). This question has an answer, under one important condition of \emph{interhorizontal complementarity}. Interhorizontal complementarity means that private horizon effects spread contagiously outward to cause social horizon effects. Your reliability invites me to become more predictable: understanding is a local public good in this sense. Such is also the chessboard problem: masters’ horizons shrink against duffers since more dumb moves are made.\(^9\) The interpersonal interdependence of planning horizons is complementary:\(^10\) you represent a disturbance term in my decision environment. We are role models for each other; we all learn through imitation: horizon effects spread through novel ideas, structures and designs. That is the nub of Romer’s (1996, p. 204) point on ‘no rival’ ideas.

So what effect does interhorizontal complementarity yield on the interrelation of prices and output? This is the key to horizontal theory: longer planning horizons – social or private – change economic relations in favor of complementarity and away from substitution: \( \text{d} S_I/\text{d} H_j^* < 0 \) in the general case.\(^11\) Simply put, horizontal lengthening alters social relations away from conflict toward a concert of interest: this is achieved through wider internalization of externalities, and through greater rationality undermining coercive force. Longer horizons expand the alignment of social and personal goals;\(^12\) they also improve ecological health through an activation of conscience, and they draw individuals into a more cooperative frame of mind (Jennings 2003). The lesson of planning horizons is the importance of complementarity in any economic culture (Jennings 2007a).

Under increasing returns in production – at least according to Kaldor (1972, 1975) – reciprocity overrules substitution in human affairs. Acknowledging ‘bits’ along with ‘atoms’ strengthens the argument too. Introducing horizon effects and interhorizontal complementarity – as a new form of interdependence – seals the case for complementarity as our dominant tie. If so, then neoclassical theory has misspecified human relations as rival, licensing competition as optimal in economics. Such should yield to complementarity and cooperation, calling for new economic conceptions and methods, some of which shall be explored.

4. \textbf{The Growth and Social Policy Implications of Complementarity}

An economics of complementarity – as a ‘positive feedback’ system – overturns some long-held techniques and doctrines in economics. Substitution, independence and additivity are not assumed; the case for competition is superseded by one for cooperation. Economic growth through learning is stimulated by reciprocity, not through rivalrous social incentives. Ecological losses show another reflection of myopia due to competitive frames. Substitution assumptions are responsible for economic crises stemming from ethical lapses, social conflict and narcissistic cultures – stimulating questions about the performance of academic communities (Jennings 2007b). Information exchanges seem more reciprocal than they are rival, implying competition in education ought to reduce social welfare: rivalry undermines complements, just like collusion of substitutes. If human relations are complementary, competition divides society and

\[^9\] This expands the number of near-move contingencies to be projected, and also weakens the planning incentives for a master player.

\[^10\] An exception could be a jealous reaction to friends’ successful learning.

\[^11\] If so, then \( \text{d} S_I/\text{d} H_j^* < 0 \): an increase in \( H_j^* \) yields – through its contagious effects on \( H_{ij}^* \) – a shift of \( S_I \) away from substitution in favor of complementarity. For any \( i \neq j \) element of \( S_I \), namely \( s_{ij} = (Q_{ij}/Q_i) \times (M_{ij}^* - P_{ij}^*) \), an extension of \( H_j^* \) will likely reduce the magnitude of both \( Q_{ij}/Q_i > 0 \) (as a weighting scalar) and \( (M_{ij}^* - P_{ij}^*) < 0 \), while increasing own-elasticity \( (e_{ij}^*) \) and thus the negative magnitude of \( (e_{ij}^* + 1) \), while the cross-elasticity \( (e_{ij}^*) \) is shifted away from substitution \( (e_{ij}^* > 0) \) toward complementarity \( (e_{ij}^* < 0) \), so \( \text{d} e_{ij}^*/\text{d} H_j^* < 0 \) as well. So regardless of the sign of \( S_I \) (as an aggregation of \( s_{ij} \) across any group \( I \) around member \( j \)), \( \text{d} S_I/\text{d} H_j^* \leq 0 \): a mutual lengthening of planning horizons shifts our relations away from substitution in favor of complementarity (in virtually all economic contexts).

\[^12\] The goal of incentive alignment applies to all levels of organization. In a business setting, “the biggest impediment to … integration of personal needs and organizational considerations lies in managers’ lack of understanding about … the ways self-interests shape … personal realities…” Two things affect the economic efficiency of all management systems and group procedures: “The concept alignment provides management with a model for understanding how individuals attempt to fuse and integrate their personal needs with the needs of the organization” (Culbert and McDonough, 1985, pp. 125-26 and 138-39; also cf. Jennings 1999, p. 69, and 2007e).
detracts from growth. Guided by orthodox economics, we are raping the earth for immediate gain at the cost of future reserves set beyond our horizon. Is it not time to address shortsightedness as an economic concern, in all its savage effects on well-being?

Economic growth is horizonal in its central lineage. Figure Two examines how an extension of planning horizons shows up in higher rates of output growth at micro and macro levels, through a number of factors already explained along with the impact of planning horizons on time-preference and discount rates. First, a longer planning horizon implies an increase of patience, so a reduced time-preference for individuals spreads across society yielding a fall in discount rates. Almost by definition, savers and lenders are more patient than borrowers, such that the process of finance is a Pareto-efficient exchange equilibrating marginal rates of impatience. Those with long horizons and ample assets will likely lend to those who want money now even at the cost of a larger payback later. Social planning horizons are reflected in ‘natural’ interest rates in free market economies. If so, then longer horizons will lead to reduced discount rates – more rapid development – ceteris paribus in nonhorizonal realms. A formalization of this analysis shows an ordinal linkage of longer horizons to lower rates of interest, thus to higher rates of growth. The whole scenario is summarized in Figure Two below.

Figure Two: A Horizonal Representation of Economic Growth

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**Legend for Figure Two**

**Case 1**: Here \((P_1^*,Q_1^*)\) is set with a short horizon \((H_1^*)\), yielding a high discount rate \((r_1^*)\), high price \((P_1^*)\) and low output \((Q_1^*)\).

**Case 2**: Here \((P_2^*,Q_2^*)\) is set with a long horizon \((H_2^*)\), yielding a low discount rate \((r_2^*)\), low price \((P_2^*)\) and high output \((Q_2^*)\).

But the observed effects are \(srQ_2^*\) which is growing at \(g_2^* > 0\) toward the ‘target’ \(Q_2^*\) at \(P_2^*\) on the long-run demand curve \(LRD\).

The macroeconomic effects operate through the impact of \(H^*\) on the discount rate \(r^*\) affecting the aggregate growth rate of \(Y^*\).

But there is another relevant aspect of horizonal growth that involves a shift from substitution to complementarity in our relations. Indeed, that horizonal lengthening augments complementarity over rivalry in our social affairs suggests that economic development transforms substitutes into complements in some mysterious way outside the purview of
orthodox standards. Such is the case in Maslow’s (1954, 1968) psychology of self-actualization, where we evolve from materialistic concerns to intangible aspirations in a process of maturation thwarted by opposition and conflict. Argyris (1971, pp. 262-63, 268-69) showed the effects of institutional leadership practices in conventional organizations that treat their members like children: mature individuals in these settings show symptoms of poor mental health, including a sense of “frustration, failure, short time perspective and conflict.” A loss of system integrity often ensues through a breakdown of vital loyalties: “The nature of the formal principles of organization causes the subordinates, at any given level, to experience competition, rivalry, intersubordinate hostility and to develop a focus toward the parts rather than the whole.”

As McGregor (1960, p. 310) reported in a well-known management theory article:

*The deprivation of needs has behavioral consequences. ... The man whose needs for safety, association, independence or status are thwarted is sick, just as surely as he who has rickets. We will be mistaken if we attribute ... passivity, or ... hostility, or ... refusal to accept responsibility to ... inherent ‘human nature.’ These forms of behavior are symptoms of illness – of deprivation of ... social and egoistic needs.*

McGregor (1960, p. 311) went on to explore the connection to rampant consumerism in a distinctly Maslowian argument on the progression of human needs from materialism to intangibles, and on the effect of frustrating personal growth through control:

*...the fact that management has provided for these physiological and safety needs has shifted the motivational emphasis to the social and egoistic needs. Unless there are opportunities at work to satisfy these higher-level needs, people will be deprived; and their behavior will reflect this deprivation. ... People will make insistent demands for more money under these conditions. It becomes more important than ever to buy the material goods and services which can provide limited satisfaction of the thwarted needs. Although money has only limited value in satisfying many higher-level needs, it can become the focus of interest if it is the only means available.*

The shift from rivalry to reciprocity due to horizonal lengthening creates a need for cooperation that – if frustrated – turns to materialism. Another way of expressing the point is that competition is keeping horizons short due to its stifling of intangible outputs such as learning, and is making us socially immature, reinforcing myopia at the expense of human development, social conscience and personal growth. Indeed, all immaterial outputs – such as love, ethics, honor, integrity and ecological health – thrive under reciprocity. All are complementary outputs stimulated by cooperation and its successful alignment of social incentives to ‘higher’ ends (in Maslow’s sense of that term). Acquisitive values are not the means to longer horizons and growth; they are a sign of competitive failure. The inefficiencies of competition appear in *horizon effects*, so elude the exclusive focus of a neoclassical lens. Substitution assumptions – simply asserted along with decreasing returns – serve us ill in this setting, though we cannot see their effect without any theory of planning horizons.

The aim of social incentive design needs to move beyond competition into a more reciprocal frame, as a means to longer planning horizons through learning and organization, by engineering a closer alignment of private rewards with public concerns. This alignment process – so well described in the management literature (e.g., cf. note 12 above) – relates not only to firms but across social systems. All living ecologies offer examples of complementary systems savaged by competition in its fragmentation of effort. There are many other realms suggesting competitive failures (still invisible in neoclassical theory) due to perverse horizon effects. All imply a need to shift away from prevailing cultural attitudes standing on substitution assumptions to a cooperative frame encouraging greater maturity and generosity. Orthodox standards in economics impose staggering costs, showing up in horizon effects.

5. **Social Welfare Implications**

So what are the social welfare implications of this approach? A high priority ought to be a lengthening of our planning horizons, achieved through a stabilization of economic decision environments – such as under rules of law rather than by bureaucratic control – and a shift from rivalrous systems to an emphasis on community, ethics and trust in culture and
organization. Acquisitive values have failed to produce social harmony and ecological health: the long-term viability of the earth is being compromised by a competitive frame perceived as socially optimal due to economists’ stubborn denial of vital lacunae in neoclassical theory. A few remarks on how an economics of complementarity invites social policy innovation toward development are appropriate, though it ought to be understood that these are only brief observations. There is work to be done. The four issues of concern are sources of social welfare: efficiency, equity, ecological health and horizontal growth.

4.a. Efficiency. Much has already been said on efficiency, on the importance of longer planning horizons for reduction of costs, so economic growth arises from better procedures and pricing cuts. But this is only a small part of what economists mean by ‘efficiency.’ In any dynamic complex system of interdependent transactions, it is the ‘fit’ of frames to their applications shaping effort to human need. A consonance of theory and use is a matter of ‘realism’ in the assumptions stating the ‘ifs’ surrounding our ‘then’ conclusions in policy choice. Substitution assumptions shall not apply in complementary settings such as in education, ecology and human relations. Competitive failures shall ensue, with outcomes straying from what we expect. This shows a need for systems approaches in economic analysis (Jennings 1999, 2007f). Perhaps an example of positive feedbacks should help present the problem. If we assume substitution and design a society on the premise that everyone has selfish intentions, such shall be the result. The very fact that we don’t look out for each others’ well-being in normal life frames social behavior into egocentric concerns, so will keep us socially immature, reducing conscience and generosity. If no one cares, we look out for ourselves. As a result, we reap what we sow. As Senge (1990, p. 274, quoting Badaracco and Ellsworth 1989) noted, the belief “that people are motivated by self-interest and by … power and wealth” is “self-fulfilling” in its effects:

> If people are assumed to be motivated only by self-interest, then an organization automatically develops a highly political style, with the result that people must continually look out for their self-interest in order to survive. An alternative assumption is that, over and above self-interest, people truly want to be part of something larger than themselves. … When organizations foster shared visions, they draw forth this broader commitment and concern.

In other words, our aspiration levels affect our behavior in profound and dramatic ways, either for better or for worse. If we expect too little then mediocrity is what we get. The fit of frames to reality – although avoided by many economists (Boland 1984, p. 174) – seems a key to horizontal lengthening and to greater efficiency. In a darkening age of anti-intellectual arrogance and troublesome methodological ignorance, it should not surprise us to find disturbing elementary errors in economic conceptions. The putative virtues of competition appear in its short-run effects, where its suppositions best apply. As soon as we step beyond the immediate term into a larger realm, microeconomic policy ought to examine entry barriers, organization and other related domains for perverse horizon effects. There is much work to be done on the efficiency implications of horizontal economics.

4.b. Equity. The equity issues so introduced also challenge orthodox standards, since a more inclusive view reveals an ethical linkage of private and social welfare results suppressed in neoclassical theory (Jennings 2005). Again, our rivalrous structures show acquisitive values and narcissism because Smith’s invisible hand deems selfishness a public good. Diminishing returns support this claim; increasing returns suggest instead that power rules over equity in and beyond the firm. But this is only a start to the problem manifest in acquisitive values, short horizons and the role of power relations in economics. Marginal productivity theory only operates smoothly in the presence of substitution and decreasing returns to scale. Among complements, some other representation of free markets applies, stated well by Nelson (1981, pp. 1053-55):

> If factors are complements, growth is superadditive. … The growth of one input augments the marginal contribution of others. Where complementarity is important, it makes little sense to try to divide up the credit for growth, treating the factors as if they were not complements. … In short, there are not neatly separable sources of growth, but rather a package of elements all of which need to be there.
In other words, when “one input augments the ... contribution of others,” these sources “are not ... separable” but must be considered together. In this situation, power rules for redistributing income at the expense of equity and the poor. Short horizons imply executive salaries are inflated, that labor – in the absence of unions – shall be exploited as well. In a less myopic world, the outcome might be different, due to a shift of values away from greed to a larger ethical realm.

Why? Longer horizons suggest a more resilient social conscience, and a recognition that our fortunes are linked in a positive way. In this situation, we will look for each other due to our understanding that in a complementary world, ‘what goes around, comes around’ too. With common interests, your misfortunes become my own as well and we thrive and decline together. Rewards in a competitive frame, maladapted to our well-being, encourage just the sort of behavior resistant to cooperation, where we all must work together on a better outcome for all. The insights stemming from complementarity open numerous avenues for reform in economics, and for research into how equity yields economic growth. These issues stand at the center of any horizontal economics.

4.c. Ecological Health. All ethical and ecological losses are horizontal, almost by definition. If what we do ripples outward forever, as is the case with complementarity, it is our range of accurate anticipation that determines well-being. An economics of substitution defines itself as short-term theory, at the expense of foresight and ecological viability. This is why economists turned away from meaningful long-term problems to narrowly-focused short-term equilibria and determinate choice. Subjectivity is excluded from mainstream models in economics; ‘objectivity’ opened a means to examine tradeoffs and draw conclusions without the confounding effect of complexity or rational limits. So ethics, organization and planning horizons are ignored, despite the enduring impact of vital living ecologies on our existence. Substitution assumptions shall not apply in complementary settings such as ecosystem management (Jennings 1999): the harm done by competition to the diversity of all life forms – so to our resilience in the face of global change – has been tragic and disastrous. So one shudders to think of future generations’ opinion of us, squandering goods in narcissistic consumption that we should keep for them, once they inherit a world deflowered by our rapacious savagery.

Substitution assumptions imply equilibrium is self-contained, so externalities simply attenuate and thus can be ignored. The reality in a complex system of cumulative causation is that spillovers grow as they emanate outward from individual acts. If so, externalities are important: the role of ethics in economics becomes central and not superfluous. Smith’s invisible hand does not work in this situation. Interhorizontal complementarity offers a nice solution to our ecological crisis if we replace substitution with integration and develop policies suited to mature adults. Such shall lend to longer horizons, so a better fit of frames to the complementary universe of all living systems in economics. An individual effort to extend one’s planning horizon will lead to contagious social horizon effects spreading outward to others. Systems should be designed to favor reciprocity over rivalry and horizons will lengthen accordingly. Too many incentive structures in neoclassical theory extol the virtues of fragmentation and disaggregation of firms (and decisional agents) in the presence of substitution, while an ecology is an integral balance of interlinked complementarities, all of whose components must be in place for the whole process to work. Cooperation is the key to ecological health, as it is to horizontal growth.

4.d. Horizontal Growth. The failures of neoclassical theory arise from its substitution assumptions standing on diminishing returns which were never more than asserted (Jennings 1985, 2007a). The ‘objectivity’ of economics (as scientific criterion) does not tally with the personal nature of human cognition (Polanyi 1958). Economics – indeed all...
learning – is subjective and open-ended; there is no way that deterministic concepts shed any insight to the analysis of volitional action in nonlinear realms. Subjective features show in every aspect of social life; failing to include them makes pseudo-scientific constructions spurious in any study of choice. Subjectivity is where we live in emotion, attitude, thought and belief; fundamental lacunae emerge without these psychological links. We achieve horizontal growth through realistic conceptual structures set in conditions that meet the facts; H* is an ordinal ‘measure of fit’ of theory to truth in particular applications. In other words, if the essential ‘ifs’ surrounding a model of outcomes hold, then that framework carries a longer horizon than otherwise. It is precisely the correspondence between our images and the reality (to which we have no direct access) that determines our planning horizons, along with the time, energy and attention that we devote to our acts.

Stable social environments – such as achieved through cooperation – allow extension of (both private and social) planning horizons in choice. Successful learning is also important to horizontal growth and may be encouraged by instituting cooperative frames in education. Indeed, the primary cause of myopia and disengagement in our economy is our system of education in its competitive values. Competition discourages output of complementary goods, such as in social learning communities. For example, look at worldwide TV programs that dismiss substance in favor of frivolous strife. Freeing economists from erroneous substitution assumptions shall lead to changes in our apprehension of social laws and their effects, specifically of planning horizons and their role in growth. This study offers only a first step to an economics full of promise for new research.

6. Summary and Conclusions

This paper reviewed the economics of planning horizons, stating a case for complementarity as the essence of human relations. Economists’ substitution assumptions have led us severely astray if increasing returns are the way of our world throughout production technology. Even without this supposition, the case for reciprocity of intangibles is strong: ideas or bits are more than ‘non-rival’; they are reciprocal and complementary in their social and network connections. Scarcity yields to abundance in this setting, calling for coordination through institutional engineering of vital living systems standing on integrative frames supporting collaboration and trust. The introduction of planning horizons and interhorizonal complementarity into this scheme makes substitution alone obsolete: the balance of substitution and complementarity among goods and activities shifts with horizon effects, either for good (to reciprocity) or for bad (toward opposition). Indeed, to know that rivalrous systems starve intangible output directs our attention to a myopic culture resulting from mainstream beliefs. Some management theory was cited to show why organizational stress shows symptoms of failure, rivalry, immaturity, conflict, disengagement, disintegration, dishonesty and myopic concerns across society, opening questions about the social impact of a competitive frame. Many insights support the economic contention that neoclassical theory – especially in its endorsement of rivalry as efficient – damages social integrity, ecological health and human well-being.

Competition is not the welfare ideal limned by orthodox standards. Sadly, it is the problem; many economists have mistaken this poison for a cure, if the ‘force locomotif’ (Romer 1996, p. 204) of growth is really horizontal in its source. If so, an economics of free markets based on competitive virtue is untenable in its assumptions. Such a conclusion opens some meaningful lessons in need of further research. For example, have economists studied the economics of complementarity in its analytical limits or requirements? The social policy implications of complementarity open a case for: role model effects; spreading ethical links; systems theory; integration; network conceptions – stretching well beyond the orthodox standards of neoclassical theory. Indeed, the favored tools of orthodoxy – additivity, econometrics, simple linear relations, static constructions – shrink in importance in any dynamic complex system. A need for more understanding of these subjects is stunningly urgent, most especially with regard to war and ecological health.

should not include man in any capacity whatsoever. This is how some came to hold that even man’s thinking is not a phenomenon. True, the ideal of a man-less science is gradually losing ground even in physics… However, for a science of man to exclude altogether man from the picture is a patent incongruity. Nevertheless, standard economics takes special pride in operating with a man-less picture. …
The ‘Washington Consensus’ said development turned on free markets, smoothly operating competitively in an open economy. Yet if increasing returns serve as our rule and not the exception, then the importance of market power, regulation and democratic control lacerate the imagined delusions of free market theory. Indeed, the elusive freedom of opportunity offered by open rivalry – in an economic context dominated by market power and other (so-called) ‘imperfections’ – simply is an illusion, just like competition is said to motivate effort and achievement though other disciplines see it differently. Economists seem to avoid difficult topics showing categorical limits surrounding conventional views, suggesting questions about our resilience in evolving global environments starved for enlightened discussion. Why are we economists so resistant to any novel departures from mainstream models and methods? Is the academic community – organized for rivalry – undermining innovation and development of ideas in its self-protective focus on traditional views (Jennings 2007b)?

Substitution assumptions shall not apply among complementarities, such as in educational, ethical and ecological applications. Selective focus entails simultaneously an exclusive blindness; theory is silent on what it ignores and we only observe opportunity costs through one theoretical lens. Substitution assumptions show collusion as socially harmful; if we never relax suppositions and test them against some alternative frame – by adopting multiple models in a pluralistic approach – then new options shall not be encountered. There is no way to examine our own intellectual limits save by exploring unfamiliar realms; single minded doctrines stay imprisoned in their own box. Substitution assumptions and their ramifications should be challenged to move beyond the competitive failures in neoclassical theory. Yet this suggests that academic communities should evolve from management systems based on competition to a more cooperative frame in order to restore resilience and diversity in their research. Otherwise substitution assumptions shall not be overturned.

The ideology of free markets should deal with its simplifications and not deny their reality. Any honest discipline ought to welcome open discussion of challenges to its central ideas, instead of forcing them out of frame. A strategy of opposition to innovation is symptomatic of a rivalrous system maladaptively imposed; the only way out of this self-contained trap is by entertaining alternatives. Social policies standing on orthodox suppositions have failed due to their improper application, nailed in place by a pattern of stubborn denial spurred by rivalrous social incentives. So would disciplinary inertia undermine development – to disastrous social effect – unwilling to fathom its own intellectual limits.

Substitution is not the only form of economic connection; indeed, it may be a special case in an open domain of complementarity. An organizational question turns on their relative force in diverse settings, such that designing institutions for efficiency is not possible without defining their relevance to any given application. ‘If all one has is a hammer, then everything looks like a nail,’ while the earth and our economy operate much more like a flower! Opposition is not the answer where human aims are aligned; the two realms of intangibles and horizons are of this sort. This is why a competitive frame may encourage short-term output at the expense of foresight, long-run growth and human development. The nature of economic relations – and their representation as substitution or complementarity – is

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The simplest way to understand why competition generally does not promote excellence is to realize that trying to do well and trying to beat others are two different things. ... Competition ... precludes the more efficient use of resources that cooperation allows. ... Beyond the greater efficiency of cooperation, it is also true that competition’s unpleasantness diminishes performance. ... At best, the stressfulness of a competitive situation causes us to try to avoid failure. And trying to avoid failure is not at all the same thing as trying to succeed. ...Competition does not promote excellence. ... Whereas cooperation apparently contributes to high self-esteem, competition often seems to have the opposite effect. ... Psychological health requires unconditionality... In competition, by contrast, self-esteem is conditional. ...Something very like an addiction is at work here...: the more we compete, the more we need to compete. ... In sum, the security that is so vital to healthy human development is precisely what competition inhibits. ...Competition does not promote ... substantial and authentic ... individualism. On the contrary, it encourages rank conformity [and] ... dampsens creativity. ... Creativity is anticonformist at its core; it is ... a process of idiosyncratic thinking and risk-taking. Competition inhibits this process ... [and] affects the personality. Turning life into a series of contests turns us into cautious, obedient people. ... The chief result of competition ... is strife.

15 As Hutchison (1977, p. 4) warned: “No kind of ignorance can be more dangerous than ignorance regarding the limits and limitations of one’s knowledge.” This sentiment was also expressed by Hayek (1955, p. 92): “It may indeed prove to be far the most difficult and not the least important task for human reason rationally to comprehend its own limitations.”
elementary in economics, so an erroneous specification thereof falsifies everything else. As Nicholas Georgescu-Roegen (1970, p. 9) warned, “the history of every science, including that of economics, teaches us that the elementary is the hotbed of the errors that count most.” Is it not yet time for renewal and to relax substitution assumptions, even to welcome a novel approach based on planning horizons? Our relative ignorance of these issues should be an impetus for research, and not for rigid denial in an economics of growth and development.

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