An Analysis and Critique of Neoclassical Economic Thought: The Pareto Principle

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*Notice: The views expressed in this Senior Integration Paper do not necessarily represent the views of Covenant College.*
Outline

I. Introduction

II. The Pareto Principle and Where it Comes From
   A. A Statement of the Pareto Principle
   B. The Utilitarian Background to Pareto: Why it was Necessary

III. The Positive/Normative Distinction
   A. What it is and How the Pareto Principle Flows from It
   B. Breaking the Distinction: A Critique of Positivism

IV. Critiquing the Pareto Principle: General Problems
   A. The Utilitarian Foundation: Preference Problems
   B. Sen’s Critique: The Impossibility of the Paretian Liberal
   C. Other problems with Pareto

V. Christian Problems with Pareto: The Wrong Standard
   A. Some Basic Christian Principles
   B. How the Pareto principle differs from a Christian view

VI. The Case Study: Debt and Structural Adjustment in Uganda
   A. Background to the Debt Crisis
   B. Uganda and Structural Adjustment
   C. Where the Christian View Differs from the Pareto principle

VII. Conclusion: Where Do We Go From Here?
   A. Is the Pareto principle inherently evil?
   B. Other Issues
I. Introduction

The prevailing theory that has driven economics over the past century is neoclassical economics. It is within this framework that textbooks and theories on the study of economics have been formulated. Economics holds an important place in our culture and our increasingly globalized world. Seemingly small changes in economic policy, such as the Federal Reserve changing interest rates, can have a large effect not just on the American economy, but on the economies of countries around the world. Economists are important not merely for the theories they develop, but also for the policy recommendations made stemming from those theories. In light of these factors, economics is certainly an area which needs to be engaged by the Christian community. However, at times the study of economics seems to be antithetical to a Biblical worldview. It has been argued that “outside the physical sciences, the social sciences are more likely to deny the role of the spiritual than the humanities and within the social sciences economics is probably the least spiritual and the most materialistic and atheistic.”\(^1\) Is there any way for a Christian to engage in a field of study which at times is atheistic in its thinking? This paper will attempt to provide such an engagement by offering a critique of the Pareto principle, which is a foundational aspect of neoclassical theory, and examining how a Christian can approach economics.

According to neoclassical theory, the Pareto criteria, or Pareto principle, offers a criteria by which to assess the efficiency of an allocation of any scarce resource. The principle, which will be discussed more fully below, basically states that a social state is Pareto Efficient when there is no way in which one individual can be made better off.

without making anyone else worse off. Neoclassical theory and many economists see the principle as “self-evidently rational.”\textsuperscript{2} Underlying the principle are several assumptions, including a positive/normative distinction and a theory of human rationality. This paper will critique the goal of Pareto Efficiency in three ways. First, it will attempt to break the positive-normative distinction. This will be extremely important because the Pareto principle flows from this distinction, allowing economists to view it as self-evident. If the Paretian principle is accepted as self-evident, then a critique of it will not be possible. However, if it can be shown that there is no such distinction, then the self-evidency of the Pareto principle can be called into question, opening it up to critique. Second, it will cast doubt on the plausibility of the Pareto principle given its assumptions. Third, it will argue that, even if the previous problems can be answered, the principle still should not be the ultimate goal of the Christian approaching economics because the foundation from which it operates is at odds with the Bible. This will obviously involve an examination of certain aspects of a Christian approach to economics. In order to illustrate this point, the paper will look at a case study that will show how a Christian approach would come to a different conclusion than a neoclassical economist. The paper will conclude by making some suggestions for improvement and arguing that the Christian can operate within the neoclassical framework in good conscience.

In writing this paper, I hope to clarify exactly what goal most economists are pursuing and why they are pursuing this goal. I hope to show that although this is not the correct goal from a Christian perspective, a Christian can operate as an economist and still remain faithful to the faith. Through the case study, I hope to provide an illustration

which will show how and why this topic is relevant and important to the average person, and why a Christian would come to a different conclusion than the Pareto principle. With these goals in mind, we will begin by first discussing what the Pareto principle is and why it was a necessary and useful development in neoclassical thought.

II. The Pareto Principle: What it is and where it came from

A. A statement of the Pareto principle

Before beginning to examine problems with the Pareto principle, it will first be necessary to understand what it is, how it was formulated, and why it is useful in the neoclassical model. The Pareto principle tells us that an allocation of resources is Pareto-efficient, or Pareto-optimal, when it is impossible to make any individual better off without making some other individual worse off. For example, say a society was in state X, and it was possible for the society to move to X1. If that move benefited at least one person, yet harmed no one, then to remain at X would be Pareto-inefficient, and the principle dictates that society will move to X1. The principle has a stronger and a weaker form. The stronger form holds that, for two states, X and X1, we should choose X1 when no one judges X to be better and at least one person judges X1 to be better. The weaker form holds that we should choose X1 instead of X when everyone judges X1 to be better.3

This will be clearer with an illustration. Assume that there are two people, Beck and Potter, and two goods, candy bars and soda. At a given state, Beck has 5 candy bars and 1 can of soda, and Potter has one candy bar and 5 cans of soda. Beck would like to have two more cans of soda, since eating five candy bars makes him thirsty, and he

would be willing to give up two candy bars to get the soda. Potter would like to have two more candy bars, because he is hungry, and he would be willing to give up two cans of soda to get them. Both parties would prefer the state where each had three candy bars and three sodas, and the weak Pareto principle would dictate that Beck give two of his candy bars to Potter, while Potter give two sodas to Beck. This would make both of them better off. Now, assume that Beck has 10 candy bars and 10 sodas, while Potter has 1 candy bar and 10 sodas. Potter would like another candy bar, and would be willing to give up a soda for it. Beck has a large amount of both, and he would be indifferent if he lost a candy bar and gained a soda. In this situation, Potter would prefer the state where he has two candy bars and 9 sodas, and Beck would be indifferent if he had 9 candy bars and 11 sodas. According to the strong Pareto principle, Beck should give Potter a candy bar in exchange for a soda, because Potter would be better off, and Beck would be the same.

It will be essential to stress the notion of “better-off” which is employed in the Pareto principle. An assumption underlying the Pareto principle is that people are rational utility-maximizing agents. Therefore, if given the choice between two states, they will choose the one which they believe will maximize their utility the most because they are rational. In the above example, Beck and Potter would trade candy bars and sodas because they both believed that doing so would make them better off. They make this choice because it is rational. After all, why would people not choose to make themselves happier if they could? From this, it can be inferred that rationality implies the pursuit of utility maximization. What this means and its implications will be examined later.
B. The Utilitarian Background to Pareto: Why it is was Necessary

The influence of utilitarianism in economics goes back to Jeremy Bentham. Bentham argued that “by the principle of utility is meant that principle which approves or disapproves of every action whatsoever, according to the tendency which it appears to have to augment or diminish the happiness of the party whose interest is in question.”4 In attempting to make a decision which would affect one’s well being, the individual should “sum up all the values of all the pleasures on the one side, and those of all the pains on the other. The balance, if it be on the side of pleasure, will give the good tendency of the act upon the whole, with respect to the interests of the individual person; if on the side of pain, the bad tendency of it upon the whole.”5 Accordingly, individuals seek after actions which will promote their pleasures and decrease their pain. This type of approach, which puts the moral weight of an action on the consequences it produces, is called consequentialism. Bentham’s account describes rational action “in terms of the mental states which result from actions, and not in terms of the desires which…provide the motive power for action.”6 This account gives reason an active role, as it becomes a rational decision to do that which maximizes one’s happiness. Bentham also argued that an individual’s utility could be quantified and added together. Under his view, all it would take to achieve an optimal social state would be to take everyone’s potential units of happiness, called utils, add them together, and choose the state which gave the greatest number of utils.7

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5 Bentham, p. 31
7 “Potential units” is used because there would be no way to evaluate everyone’s actual units until after the action. If actual units were used, there would be no way to make any kind of social decision, because one could not evaluate it without deciding, and one could not decide without an evaluation.
There was an initial reaction to Bentham’s view due to its reduction of man to a pleasure-seeking magnet. John Stuart Mill attempted to redefine pleasure such that it took into account the happiness of others. For Mill, people ought to act in such a way as to improve the happiness of society as a whole, not merely the individual. Others took this approach and used it explain other aspects of life. For example, the Chicago school of economics has used the approach to explain marriage in terms of the utility one derives from it. A problem arose in that eventually, utility could be used to explain everything, and the theory degenerated into a tautology. As a result, Bentham's view returned to the forefront.

A major concern for the economist with a utilitarian foundation was how to quantify utility and to compare it between people. If this was impossible, then utility theory was much less useful for economic predictions. Some have argued that, due to this inability, “there is no effective theoretical or empirical standard with which to gauge utility, and therefore, has been no successful demonstration that any market has functioned so as to maximize utility.” This type of argument may apply to cardinal utility, but it ignores another development in economic thought. Economists avoided the problem of quantifying utility by moving from a cardinal to an ordinal type of utility. The Italian economist, Vilfredo Pareto, was one of the first to make this move. In his view, cardinal utility was a mere representation of preference ordering. Under an ordinal, or preference-based view, the individual was thought to be able to tell whether or not he desired a certain outcome more than another one. The individual had preferences between differing situations, and acted based on those preferences. Pareto used the concept of indifference curves. An indifference curve is a set of goods and services
between which the consumer is indifferent. The individual seeks to move to the highest possible curve, representing the highest amount of goods and services possible, given his budget constraint. In this way, the preference-based view allowed comparisons of differing allocations of goods and services for the individual.

One problem remained, and that was interpersonal comparisons of utility. There was still no way to make such a comparison, and for fairly obvious reasons. Say there are two individuals, A and B, who can choose between two goods, X and Y. Perhaps both A and B prefer X to Y. However, there is no way to know which one prefers it more, because there are no numbers to base such a comparison. The Pareto principle is the answer to this problem. It provides a criterion to judge the social efficiency of any allocation of goods and services without making interpersonal comparisons of utility. It is an extremely important feature of neoclassical thought, and not just for the judgments it allows economists to make.

In the neoclassical model, “competitive equilibria without externalities, public goods, informational limits, etc. are, by the first welfare theorem, Pareto efficient.”9 The first welfare theorem simply states that competitive equilibria are efficient. Therefore, in the neoclassical model, an efficient economic outcome will occur through the workings of a competitive market. This provides the reason why we should have competitive markets: the less restriction placed on the market, the more efficient it will be. In this way, the Pareto principle provides the justification for the competitive market. Since it is seen as self evident, it allows the economist to theorize about allocations and judge between different allocations according to their Pareto optimality. With the Pareto

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9 Hausman and McPherson, p. 702
principle, the economist can “with no ethical premise more controversial than minimal beneficence…offer moral evaluations along one single dimension.”\textsuperscript{10} The perfectly competitive market is good because it is efficient, and market failures are bad. Pareto optimality is the goal of any set allocation of resources, because a Pareto optimal state is one which is efficient and where there is no waste.

\section*{III. The Positive-Normative Distinction}

A. What it is and how the Pareto Principle flows from it

A positive statement is a statement of what is. Such statements describe the way things are and make no value judgments. The statement “it is raining” is a positive statement. It is describing a state of affairs without appealing to any value system. It may be true or false, depending on whether or not it is, in fact, raining, but it can be verified without appealing to values. Normative statements are ones which concern the way things should be; they make value judgments. The statement “you should obey God” is normative in that it prescribes how one ought to live. This is the key between positive and normative statements: positive ones describe the way things \emph{are}, while normative ones describe the way things \emph{ought to be}.

The implication for economics is as follows. Positive economics “is concerned essentially with questions of how the economic system operates and what results might be expected to follow if actions of certain kinds are taken.”\textsuperscript{11} Normative economics “is concerned with what, against certain established criteria, ought to be.”\textsuperscript{12} Neoclassical economics claims that “it is a value-free, morally neutral science that simple describes, in

\textsuperscript{10} Hausman and McPherson, p. 702
mathematical terms, the way things really are.”13 The neoclassical economist places his field in the same arena as the physical sciences. In his textbook, *Economics*, Richard Lipsey says that “economics, like other sciences, is concerned with questions, statements, and hypotheses that could conceivably be wrong (i.e., falsified) by actual observations of the world . . . thus an appeal to facts is an appropriate way to deal with them.”14 Economics, since it is assumed to be a science, can then be studied “with the same objective detachment used by the chemist probing the molecular structure of sodium.”15

Accordingly, economists claim that their work involves no normative statements. It merely describes the way the world works, not how it should work. Later in his textbook, Lipsey states that “it is possible and fruitful to distinguish between positive and normative statements.”16 At this point, one might ask “how is it possible, then, for the economist to be involved in policy? With all of the headlines about the economy and quotes from economists stating which policies would work to achieve such and such goal, how is this positive-normative distinction maintained? The economist would answer that “the relevance of economics is purely technical. It provides causal knowledge of policies to allow policymakers to choose effective means towards their ends. Ethics determines the ends, and economics determines the means.”17 In this way, the economist believes that he can preserve the distinction and still be involved in policy, although this point will be disputed below.

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12 ibid., p.70
16 Lipsey, p. 18
The Pareto principle flows from this distinction. As mentioned above, the principle is assumed to be self-evidently rational. However, at first glance this seems to be obviously false. If the economist argues for Pareto Efficiency, then is he not making a statement about how things ought to be? Is arguing that we should move from Pareto-inefficient to Pareto-efficient states making a value judgment? The economist attempts to skirt this by saying that the principle is one which is commonly accepted in the real world. According to neoclassical theory, the Pareto principle is an “innocuous and uncontroversial moral principle.” Who would argue that, if it is possible to make someone better off without making anyone else worse off, then the person should not be made better off? Is not this idea just a self-evident feature of reality? Even from a Christian point of view, this makes sense. Why should we not allocate resources so that more people are better off? In fact, the principle fits with Scriptural injunctions against waste. At this point, the principle seems like it is self-evident, and the economist is able to avoid normative statements in abiding by it.

B. Breaking the Distinction: A Critique of Positivism

The positive-normative distinction has drawn much criticism, from both secular and religious sources. While Christians such as A.B. Cramp have argued that “this detached, scientific pose of modern economics is almost wholly bogus,” non-Christians such as Hausman and McPherson have argued for a similar thesis. In their desire to be a science, economists have claimed value neutrality. However, according to the critique, what they have in fact done “is to conceal the valuations that underlie their analytical

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18 Monsma, George. *Normative Economics*, p.169
19 Hausman and McPherson, p. 675
structures—and, indeed, the very terminology they use—so deeply that they can happily remain unaware of them in their researches and trust the latter are merely factual.” If this is true, then what remains is to unearth these valuations from within neoclassical theory, which is what this section will try to do.

In its desire to be a purely positive science, economics has “been founded upon the generally accepted presumption that the investigatory techniques used…in the physical sciences are readily and with only minor modification applicable to the study of human interaction in the marketplace and elsewhere.” This presumption leads the economist to believe that the study of economics can be done with the same objectivity as a scientist. Economics is sometimes called “the science of choice,” and the economist believes that his work, since it uses a similar methodology as a physicist’s, is value-free. Therefore, it would be reasonable to assume that, if scientific methodology contains normative elements, then the study of economics is not free from them either. This is the course the critique will follow.

The physical sciences are commonly thought of as objective investigations of the world. Nowhere is the positive-normative distinction more prevalent than in the scientific method. However, this objectivity of science is not as objective as it first appears. The scientific perspective depends on a special view of nature and man which carries normative implications. In approaching the universe, the scientist seeks understanding, and expects that the area being studied can be understood. This concept of understanding, of discovering the latent laws of nature which give order to an

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21 see Hausman and McPherson, p.673
23 McKenzie, p. 57
otherwise chaotic universe “necessitates a willingness on the part of the observer analyst to take the position that order can be found in apparent chaos.”25 Already, the scientist has moved away from objectivity; the drive for understanding has led to a presupposition that there is some sort of order to be understood. This goal of science leads to a foundational view of what the world should look like, and it is hard to see how “such a commitment can be anything other than normative, founded in much the same spirit that people believe in God.”26 If this is true, then science is foundationally normed in that it assumes that the universe should be orderly, leaving it up to man to discover the nature of this ultimate order.

Perhaps, though, one could argue that understanding does not play as big of a role as has been presented above. Maybe the scientist is able to approach the study of reality with a clean slate and come at the world objectively. There is, however, one problem with this idea. If the scientist faces the “spray of phenomena” that is reality without any type of methodology or framework in place, then is it possible to learn anything? When one faces reality as a “scientific virgin”27, where can one start without imposing some kind of framework on the universe? In order to begin learning, some type of normative element must help determine what one should attempt to learn.

This can be applied specifically to economics in looking at how an economist chooses what to study. When doing research, the economist must make some type of value judgment in selecting “what area to study, which data are relevant, which theory to

25 McKenzie, p.60
26 McKenzie, p.60. Of course, a Christian would argue that God is the reason why man has this drive for order and understanding. Since we are created in His image, and He is the ultimate order to reality, then we will naturally seek order in the world around us. However, the critique is attempting to answer the positive-normative distinction without explicitly bringing in religious concerns. A section below will deal with a Christian response to economics.
select of the infinite number that are consistent with the data, and which method to use to validate the theory.” 28 Each step of economic research inherently involves some type of decision requiring choosing an element to the exclusion of others. This involves placing a higher value on some elements than on others, which involves having reasons why this or that element should be in the study, or why this or that theory should be used.

Other normative elements begin to come into play as well. The methodology of science places high value on things like curiosity, measurement, quantification, observation, experimentation, and objectivity, and economics is no different. The scientist accepts empirical verifiability as the basis for judging a theory’s usefulness and simplicity. However, it has been acknowledged that “the gains from greater accuracy, which depend on the purpose in mind, must then be balanced against the cost in achieving it.” 29 Basically, the scientist must sometime choose between a model which yields more accurate results but is very complex and one which is more simple but not quite as accurate. How could this be done without appealing to some type of normative criteria? From the foundation up, the scientific method places values on aspects of reality, making it inherently linked to the normative. If economics is to be viewed as a science, then it will come up against the same problems as science in attempting to maintain a positive-normative distinction.

How does this affect the Pareto principle? If there is no positive-normative distinction, then economics is no longer wholly objective. It necessarily involves value judgments in many of its aspects. If the distinction from which the Pareto principle flows

27 McKenzie, p. 65
28 Tiemstra, p. 237, see also Vickers, p. 67
no longer exists, then it is possible that the principle is no longer as self-evident as it earlier appeared. If the Pareto principle involves an underlying moral foundation, then the door is opened to examine that foundation and, if necessary, critique it. The question now becomes whether efficiency is a universal value which should be pursued before all else. While the neoclassical economist believes this, there are many who do not, especially in Christian circles. From a Christian viewpoint, issues such as justice, stewardship, poverty, or rights may be as important if not more important than efficiency. One has to look no further than authors such as Goudzwaard, Monsma, or even Sen to understand that efficiency based on individual preferences is not a universal value, and as such it cannot be a self-evident truth about reality. From here, we can move on to examine specific problems with the Pareto principle, each of which give reasons to think that it is not a self-evident feature of reality.

IV. Critiquing the Pareto Principle: General Problems

A. The Utilitarian Foundations: Preference Problems

While the Pareto principle avoids several problems associated with its utilitarian foundations, there are still several issues which it must deal with. Most have to do with the idea of the individual’s preferences being the foundation for the individual’s utility, while some deal with the linkage between rationality and preference choice. Preference-based utility relates to the Pareto principle because a social state is deemed Pareto efficient when there is no allocation which makes someone better off without making someone else worse off. It is important to realize that the “better off” has to do with what the individual prefers. If a utility maximizing individual preferred a certain state to the status quo, and if it were possible to get to this state without making anyone else worse off, then
it would be Pareto inefficient not to move to that state. Individual preferences play a foundational role in determining Pareto optimality.

However, preference-based utility is not without its problems. One problem is that preferences may be based on false beliefs. To use a simple example, say that Stan believes a certain glass of liquid in Suzy’s hand is water and will therefore quench his thirst. Suppose, however, that the glass actually contains a fatal poison. Would Stan be enhancing his welfare by drinking this glass? Or, to take the illustration further, what if he thought it would make him immortal?\footnote{While this may at first seem ludicrous, if one stops to consider the crazy things that people in cults or even mainstream religions have done over the last decade, it begins to seem less farfetched.} Should Suzy allow him to drink it? While this takes the idea to the extreme, there are often instances where someone may, due to a false belief, prefer something that may end up causing harm.\footnote{Hausman, Daniel, and Michael McPherson. “Preference, Belief, and Welfare” The American Economic Review v.84, n2, May 1994, p.396} As a result, many who link well being with preference satisfaction require the assumption that the individual has perfect information, thus grounding preferences in true beliefs. This assumption has its own problems because it is questionable that any individual always has perfect information in an economic situation, bringing into question how well the theory matches up with the reality it is trying to describe.

Another challenge facing the preference-based view has to do with how an individual views his current situation, and this problem could apply even if everyone had perfect information. For example, “a person who is ill-fed, undernourished, unsheltered and ill can still be high up on the scale of happiness or desire-fulfillment if he has learned to have realistic desires and to take pleasure in small mercies.”\footnote{Hausman, Daniel, and Michael McPherson. “Preference, Belief, and Welfare” The American Economic Review v.84, n2, May 1994, p.396} On the contrary, someone who is materially well off may be miserable due to different preferences. Who
is truly better off? Under the preference-based view, we must say that the first person’s well being is greater than the second’s, since his preferences are fulfilled. Why is this important? Could the neoclassical economist simply argue that this is outside of his field of study, that all he can do is tell how to allocate resources efficiently? The reason this point is important for neoclassical thought is that the neoclassical tends to associate betterment with increasing physical commodities, yet still relies on a standard for well being which depends not on a physical condition but a mental state. Since utilitarianism is a foundation, the neoclassical model is inevitably linked with the psychological. The following illustration will help explain why this point is important.

Imagine that there are two children from two wealthy families. The parents of both children earn the exact same income, they have the exact same houses, and they are equally loving parents. In fact, imagine that the children are equal in every way. They have the exact same toys, clothes, etc. Now, suppose one day that child A’s parent buys child A an expensive new video game system. When child B sees child A’s present, he strongly prefers to have one. When he asks his parents, however, they tell him he cannot have one. So, in his mind, his welfare has decreased even though he has lost nothing, and according to a preference-based understanding of well being, he is now worse off than before. Now, take this idea and expand it to a perfectly competitive market which is growing at a high rate. It may be possible that “as the level of production, advertising, and consumption of goods in a person’s society rises, he [the individual] may well perceive himself to be worse off than before, if his own consumption remains constant. In such cases, even perfectly competitive markets will fail to give Pareto optimality.”

33 Monsma, p. 174
This would violate the first welfare theorem, which says that perfectly competitive markets are Pareto Efficient. In this situation, by increasing production, one person is made worse off since he is worse off in his own mind, and the market therefore creates an inefficiency. This is certainly a scenario not in accord with standard theory, which sees growth in production and consumption as the keys to happiness.

A third and final issue dealing with the utilitarian foundation of the Pareto principle has to do with the explanatory power of the theory. According to its foundations, individuals are rational utility maximizing agents. Some have taken this and used it to argue that any individual action is one of pursuing utility maximizing. Using this, they explain everything in terms of utility, even acts of altruism or charity. This has been sharply criticized from many different sources. Some argue that this idea does not fit with reality: “compassionate acts commonly go beyond utilitarian altruism, reflecting a moral assessment of what acts are intrinsically right, regardless of the consequences.”

Paul Samuelson, whom many consider the father of modern neoclassical economics, scoffs at the idea, saying “such argument is not even wrong. It is just boring, irrelevant, and in the technical sense of old-fashioned logical positivism, ‘meaningless’.” A.B Cramp goes a step further, arguing that such a move puts one “in the position that ‘utility’ is an umbrella word for ‘anything which moves us to action’, in which case it explains nothing.” If utility and preference satisfaction is used to explain everything, it becomes a tautology and therefore meaningless. One ends up arguing that people are rational utility maximizers because that is how they are defined. This destroys the explanatory

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power of the model, and therefore hurts the explanatory power of the Pareto principle which is based on this framework.

While these three issues do not destroy the Pareto principle, they represent potential problems, some of which have been dealt with and some of which need to be dealt with more deeply. However, we will leave utility for now and move on to a more technical problem involving the Pareto principle and individual liberty.

B. Sen’s Critique: The Impossibility of the Paretian Liberal

Amartya Sen’s famous “Paretian liberal” paradox attempts to show a conflict resulting from the Pareto principle and a condition of individual liberty. According to the paradox, “an apparently weak, necessary condition respecting individual liberty—that two individuals be decisive over their own single pair of alternatives, which differ only with respect to some purely private matter—is incompatible with the achievement of Pareto optimality when people hold certain plausible rankings of social alternatives.”

Sen’s paradox follows up on another famous paradox, Arrow’s General Impossibility Theorem.

Sen’s paradox follows a method similar to Arrow, and since it relates much more specifically to the Pareto principle than Arrow’s theorem, it will be the subject of focus. The paradox is fairly technical, and a simplified version will be presented here. Before presenting the paradox, the elements which make it up will first be presented.

A social decision function determines a complete and consistent social preference defined over the set of alternative social states for any n-tuple set of individual preference orderings. This function has an unrestricted domain when every logically possible set is

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36 Cramp, p. 56
37 Hausman and McPherson, p. 715
included in the domain of the function. This condition will be called Condition U. The condition of *minimal liberty* (ML) stipulates that at least two people in the society have a recognized personal sphere in which their preferences and theirs alone would count in determining the social preference. For example, if individual X wants to sleep in a certain position, then this preference, since it falls within his private sphere, should determine society’s preference for this case. Since what position he sleeps in does not affect anyone else, then society should allow his preference to count as its preference in that case. The weak version of the Pareto principle, called Condition P, is also used. As stated above, the weak form states that, for two states X and X1, X1 should be chosen when everyone judges X1 to be better.

The paradox is that there cannot exist a social decision function which satisfies Conditions U, ML, and P. It is also assumed that, in choices over the individual’s personal sphere, the individual will choose entirely according to preference. So, if individual 1 prefers x to y, and they are both in his personal sphere, he will never choose y when x is available. In this situation, x will be better than y according to his own preferences.

So, how exactly does the paradox work? Showing the paradox will be aided by the use of an illustration.38 Suppose that there are two people: Person A and Person B. Both of them prefer having a full-time job (1) to a half-time job (1/2), and a half-time job to no job (0). However, neither person cares for the other, so much so that each prefers that the other be jobless. In fact, they both would get more satisfaction the level of the other’s unemployment than at the level of their employment. Now, suppose that there are

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four possible states of jobs for A and B. Each state is represented by four pairs. The first number in each pair describes A’s job situation, and the second describes B’s. The preferences of each individual would be as follows:

<table>
<thead>
<tr>
<th>Person A</th>
<th>Person B</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1/2, 0)</td>
<td>(0, 1/2)</td>
</tr>
<tr>
<td>(1, 1/2)</td>
<td>(1/2, 1)</td>
</tr>
<tr>
<td>(0, 1/2)</td>
<td>(1/2, 0)</td>
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<td>(1/2, 1)</td>
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</tbody>
</table>

So, for the first pair in Person A’s ordering, 1/2 represents A’s job situation, and 0 represents B’s. For the first pair of Person’s B’s ordering, 0 represents A’s job situation, and 1/2 represents B’s. In order to meet Condition U, the social choice function must contain each ordered pair ordering above. If we assume ML, then A’s personal sphere would cover (1, 1/2) and (0, 1/2), and B’s would cover (1/2, 1) and (1/2, 0). Each individual, according to ML, should be free to work if he prefers, given the job situation of the other.

So, according to the principle of ML, (1, 1/2) is put over (0, 1/2), because A prefers (1, 1/2), B is not directly involved in A’s decision, and (1, 1/2) falls within A’s personal sphere. On similar grounds, (1/2, 1) is put above (1/2, 0).

Now, if we are to observe the Pareto principle, then (1/2, 0) must be put above (1,1/2), because both A and B prefer (1/2, 0). Also, (0, 1/2) must be placed above (1/2, 1), because both A and B prefer this. The reason for this goes back to the statement above that each gets more satisfaction at the level of the other’s unemployment than at
the level of their own employment. Person A would rather work part-time than full-time if it meant that person B worked less, and the same goes for person B.

When these two conditions are combined, we get the following preference order:

(1, 1/2)
(0, 1/2)
(1/2, 1)
(1/2, 0)
(1, 1/2)

This ordering meets Condition U, because every possible ordering is included. However, there is a problem in that every state is worse than some other state. There is no way to determine which state is the best one based on the preferences of the individual.

This is a rather remarkable result, and it has generated volumes of literature attempting to find a way out of it. What are the implications of this theorem? Sen argues that “there is nothing much to ‘resolve’ anyway. The impossibility of the Paretian liberal just brings out a conflict of principles—a conflict which might not have been immediately apparent.”

These principles have to do with giving priority to preferences over personal spheres and accepting the Pareto principle. Necessarily, “the conflict arises only with particular configurations of individual preferences,” and it may not apply.

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39 Sen, “Liberty and Social Choice”, p. 28
when individual liberty rests on values respecting one another’s personal spheres instead of certain rules of social choice. However, it can pose a problem under certain conditions. Sen’s point is that the condition ML seems like one which everyone would except. We all believe that there are areas which should fall solely within our personal spheres. If the economist accepts this seemingly obvious condition, then at times he will face a challenge: can he have liberal values and the Pareto principle? And, if there are cases where he cannot, then which one will he get rid of?

C. Other problems with Pareto

While Sen’s paradox involved some abstract and technical reasoning, this section will deal with some Pareto issues which are less complicated and more obvious. The foundational complaint that will be lodged here has to do with questions of distribution and how they effect the Pareto principle.

However, before moving to these complaints, there is one issue worth mentioning, not as a problem per se, but as something that must be clarified when dealing with the Pareto principle. This issue is how far the principle should cover. Do we seek Pareto optimality on a local, national, or international scale? How one answers this question could greatly impact how one is able to use the principle. There are allocations which may be good for the U.S. and would be Pareto-efficient if the principle were applied on a national scale, but harm millions outside of our borders and are therefore Pareto-inefficient on an international scale. Also, if we are dealing in the international arena, or even a national arena, we must ask whether the principle is feasible. Some have argued that the principle “has very limited applicability, as economic changes usually involve
In this age of increasing globalization, the effects of the slightest changes can be felt around the world, and it may be difficult for any type of change to be Pareto-efficient. In dealing with the Pareto-principle, it will be helpful to identify which arena one is discussing, and to also address the applicability of the principle given the arena chosen.

While the Pareto principle provides a criterion for allocation of resources, it remains silent on distribution issues, which can leave it as a weak criterion for efficiency. Any state in which it is not possible to make someone else better off without making someone else worse off is Pareto efficient, which means that there are endless possibilities of Pareto optimal states, all with differing distributions. The principle provides us with no mechanism to choose between different states. Suppose that we have two states. In state A, everyone is totally equal in every way, and there would be no way to change things to better someone without hurting someone else. In state B, one person gets everything and all others get nothing. According to the Pareto principle, both states are optimal, because it would be impossible to make someone better off without making someone else worse off. The principle in and of itself says nothing concerning which of these states is better, making it somewhat weak as a criterion.42

There have been attempts to fix this problem by proposing ways to compensate the losers from the winners’ gains. The idea would be to make a change, then take some from the winners of the change and give it to the losers, thus increasing the welfare of everyone. One example would be to tax the winners and give something back to the

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41 Hausman and McPherson, “Taking Ethics Seriously”, p. 702
losers. While this sounds like a good idea, it faces many challenges. First, there is a question of whether the idea is feasible. It may be practically impossible to make a policy change, identify every individual who benefits and how much they benefit, identify every individual who loses and how much they lose, then make a redistribution from there. The costs and time would be enormous, especially as we moved to a national and international scale. This scenario might also necessitate quantifying the amount of gains or losses, a step which faces the problems of quantifying utility (see Section II above).

A second issue is whether an economist could recommend such a redistribution and remain morally neutral. It would be difficult to maintain the positive/normative distinction yet endorse a redistribution, because doing so would suggest something fundamentally good about equality, which would bring normative content into the picture. An illustration from the Third World debt crisis, which will also be presented in the case study, will help explain this argument.

In the 1980s, many developing nations were in massive debt which was wrecking their economies. In most nations, there were strict government controls and regulations on both trade and domestic production. These regulations meant that most developing nations were in Pareto inefficient states. We will call this state A. The neoclassical prescription to get them out of debt was to get rid of regulations and open up their markets, which would allow resources to be allocated efficiently. Thus, many developing nations were forced to implement Structural Adjustment Policies (SAPs), which were designed to let the market work and achieve efficiency. They worked in that efficiency was achieved and growth began to occur in many countries. We will call this state B.
However, at the same time, they hurt the poorest people in those nations the most. Why this occurred will be explained in the case study, but for now, it is enough to know that the poor bore the biggest burden from SAPs. Inequality in many countries went up. Ideally, the best way to overcome this would have been to tax those who won from the changes and set up safety nets for the poor. We will call this state C.

In the example, states B and C are both Pareto efficient in that resources are allocated efficiently, and both are preferred to A. However, there was no way to get from A to C directly, because growth had to occur, and the quickest way for this to happen was to open up the markets. So, countries had to move from A to B. There were many who wanted to move from B to C, because they realized that the poor had been hurt by SAPs, and they wanted to come up with some type of redistribution to help them. According to the argument in the previous paragraph, the neoclassical economist could not recommend this move from B to C, because doing so would imply a notion of equality and bring normative content into the picture, thus violating the positive/normative distinction. Due to the structure of the Pareto principle, questions of distribution cannot be addressed.

This third challenge for redistribution provides the basis for another general issue for the Pareto principle. The principle compares positions which are static. The question posed by Pareto asks whether at least someone is better off and no one worse off at equilibrium position B compared to equilibrium position A. However, “little or nothing is said about the actual costs of the movement from one equilibrium position to another.”\(^{43}\) If these costs were included in the analysis, the change may no longer be Pareto efficient. While this is not necessarily the case, the fact that these costs are not

\(^{43}\) Nelson, Robert H. *Economics as Religion*, Pennsylvania State University Press, University Park, PA, 2001, p. 82
even considered is potentially troubling. At the same time, one must realize that the principle is part of an economic model of reality. The issue is not whether the model mirrors reality exactly, but whether the resemblance is close enough that predictions can be made. We should not expect the model to include everything, and it is probably safe to ignore transitional costs in the case of the Pareto principle since each individual probably figures them in when determining whether he/she will benefit from a certain change.

Before moving on to some specifically Christian problems with the Pareto principle, it will be helpful to return briefly to the question of distribution, because the issues raised there indicate both the root problem of the principle for a Christian as well as a potential solution. While many understand that distribution is a key problem for Pareto, neoclassical theory is unable to explain why without violating the positive/normative distinction. Even though some schemes of redistribution have been proposed, many have been hesitant to endorse them because to do so would imply that, at times, the market yields unfair allocations which should be amended. Admitting this would bring normative content into the discussion, and the faithful scientist of choice is loathe to do this. However, if one would allow normative content into the discussion, the results could be much different. The next section will look at some Christian problems to Pareto and begin to explain the merits of an end to the positive/normative distinction.

V. Christian Problems with Pareto: The Wrong Standard

A. Some Basic Christian Principles

Before discussing how the Pareto principle as a neoclassical criterion is at odds with a
Biblical worldview, it will be helpful to first briefly lay out some Christian principles with which the Pareto principle can be compared. These principles can be divided into four areas: stewardship, poverty, materialism, and work. While this will by no means provide an exhaustive account of a Christian economics, I hope to merely lay out some foundational principles that any Reformed believer would agree with. While the mechanisms or outcomes within each area may be disputed among believers, the principles behind them are more obvious, and as such can function as a type of common starting point from which we can evaluate the Pareto principle. In this section, the basic principles will be laid out. The next section will discuss how the Pareto principle relates to these principles and is in conflict with them.

The first principle is one of stewardship. While God has ultimate control over all areas of life, he has set man to be his steward over aspects of creation. He does this early on in Genesis, telling Adam and Eve in the cultural mandate: “Be fruitful and increase in number; fill the earth and subdue it. Rule over the fish of the sea and the birds of the air and over every living creature that moves on the ground…I give you every seed-bearing plant on the face of the whole earth and every tree that has fruit with seed in it.”44 We clearly have a special place in creation and are given rule over creation. However, this does not mean that man can do whatever he wants. He is accountable to God for his actions, and his ultimate purpose is to glorify God. This means that man’s ultimate purpose is normative. Man’s actions either bring glory to God or do not. If man’s purpose is to glorify God, then there is no such thing as a positive/normative distinction.

The aspect of poverty is one which Christ mentions often, but is found throughout Scripture. In the Bible, “there is a clear obligation for believers to see to the needs of the
poor.” This can be seen in Old Testament laws to help widows and orphans all the way up through the teachings of Christ and into the apostolic writings. The poor have a special place in God’s heart, and it is the duty of the believer to have a concern for them and help them. While the causes of poverty and possible solutions are sources of dispute, the principle of caring for the poor is not.

A third area to be discussed is that of materialism. Scripture speaks about material wealth in many places, most notably Proverbs and the Gospels, and “while the Bible makes it clear that wealth is not a bad thing in itself, and may indeed be a blessing from God, placing hope and trust in material prosperity is a form of idolatry, and hence inappropriate for believers.” This latter part of the statement defines what materialism is: the belief that material things are the keys to happiness and solving problems. The Bible condemns this belief since it elevates material positions above God.

A final area that I wish to mention is that of work. Work is something that is both commanded and approved of by God. In the Bible, “work is the appropriate Christian response to the cultural mandate, and people ought to ordinarily support themselves by working.” I would go one step further and say that, not only ought people to work, but they have a right to work and to be able to support themselves through that work. This principle goes back to the cultural mandate in Genesis 1:28, and it can also be seen in Old Testament laws which allowed the poor to pick gleanings of wheat from a rich person’s field. In the Old Testament, the poor were not merely given handouts, but were required to work to gather them. Also, they had a right to do this by the law which God gave

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44 Genesis 1:28-29
45 Tiemstra, p. 228
46 Tiemstra ,p. 228
47 Tiemstra, p. 228
them. From this situation we can see that man ought to work and has a right to work and support himself though that work. There will be times when people are unemployed, such as when they are changing jobs. The unemployment rate in a country will never be zero. The problems with unemployment come when there are people who want to work and cannot as well as when there are people who are capable of working but simply do not want to. Unemployment is evil because it prevents man from doing that which he is called to do: work.

B. How the Pareto principle differs from a Christian view

A first set of problems has to do with the idea of individuals always making choices according to their preferences. The economic view of man in the Pareto principle is that he a rational utility maximizer. Rationality is defined as utility maximization. This is seen as self-evident, that the individual would choose that which made him better off instead of worse off. The ideas of morality, rights, or compassion are not explicit in the neoclassical formulation of how man acts. In the model, focus is placed on the ends, and not the means. The question asked in the neoclassical model is “Is the end result Pareto efficient?” This could come into conflict with the Christian view in several areas. For example, assume a certain allocation will create unemployment in the short run. The economist would say that the government could compensate those who lose their jobs with money from taxes until those people find new jobs, which they eventually will. The neoclassical model says nothing about man’s right to work, nor does it say anything about whether or not it was just that the individual should have his job taken away from him. This is unimportant because it is assumed that the allocation will lead to increased

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growth, and that since the individual will eventually find a new job, this is Pareto-efficient.

In the neoclassical model, the ideas of rights, morality, altruism, or compassion are rarely included in the analysis of choice. This is an inadequate depiction of man, as it reduces him to one facet: that of a utility maximizer. While it is true that man often acts to maximize his utility, there are times where other motives may come into play. To reduce man to one facet is to ignore other dimensions of him which come from being made in God’s image. Also, the focus on ends prevalent in this formulation conflicts with a Biblical view, which often emphasizes means as much, if not more than, ends. In the Pareto principle, what matters is that the state society ends up at is Pareto optimal. However, it makes no mention of appropriate ways to get there. Nothing is said about what happens in the interim as an economy moves from one state to another, if the process is one which is right or just. The emphasis is placed on the end results: are they efficient?

The Pareto principle argues that any allocation of resources is efficient if it impossible to make someone better off without making someone else worse off. This in and of itself may not be bad. However, as has been discussed above, “better off” means better off according to the individual's preferences. The individual and his preferences become the ultimate standard for choosing the best allocation of resources. There is a basic error here.

We know that the individual is sinful. This state of man “distorts both our evaluations of what is best for ourselves, and our actions…Sin also causes us to desire
things contrary to God’s law, and to act on these desires." 49 Because we are sinful we sometimes desire things which are either morally wrong or harmful to us, or both. For example, in a drug deal between a dealer and a heroin addict, both parties perceive that the transaction benefits them. According to the Pareto principle, then this transaction could take place. If it is prevented, then an inefficiency is created. While we obviously have laws against some things which we deem harmful, I would argue that we have them due to certain common grace insights which come from man being made in God’s image. In a purely economic sense, they create an inefficiency. One might argue that these are there because there are certain things which we obviously should not do, but the economist is not allowed to say this without breaking the positive/normative distinction. Because the Pareto principle makes fallen man the ultimate standard, it is a standard that is foreign to biblical Christianity.

In summing up this section, there are two key areas where a Christian would have problems with the Pareto principle. The first is that the formulation of man as a rational utility maximizer upon which the principle is based does not adequately address issues such as rights or morality. This is due primarily to the utilitarian ethic underlying neoclassical theory which dictates that more emphasis be placed on consequences instead of procedures. Second, the Pareto principle starts from a place which is fundamentally unbiblical: the fallen individual. Man is the ultimate judge of what makes him better off. It is assumed that he will make himself better off by consuming more, and this becomes the focus of economics: growth. Questions of distribution are overlooked, and as such the poor are often neglected or taken advantage of. As we shall see in the case study, often a Christian view of economics would make a much different recommendation than

49 Monsma, p. 171
an economist operating from the Pareto principle. I hope that the case study will provide an illustration of some of the points that have been discussed thus far.

VI. The Case Study: Debt and Structural Adjustment in Uganda

A. Background to the Debt Crisis

In order to understand what happened in Uganda, it will be helpful to discuss the general features of the Third World Debt crisis, which began in the 1970s and remains a problem today. From there, we can look at some features unique to Uganda which contributed to its crisis, as well as the reforms it implemented and their effects. The study will conclude with a section of where an economist operating from a Christian framework would have come to different conclusions than the neoclassical model.

In the early 1970s, many developing countries were growing at impressive rates. In order to maintain this growth, “many countries had begun importing heavily, especially capital goods, oil, and food.”50 In 1974, OPEC cut its supplies of oil, which meant that oil prices around the world went up, and that there was a worldwide recession, which meant the demand for products from developing nations went down. In the face of these two factors, “many developing countries sought to sustain their high growth rates through increased borrowing.”51 They needed loans because their exports decreased and the price of their imports had increased. When OPEC countries cut supplies and increased profits, they deposited the money in Western Banks. Banks therefore had more money on hand and a decreasing domestic demand due to the recession, and they therefore “aggressively competed in lending to developing countries on comparatively

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51 Todaro, p. 553
permissible and favorable terms." The total external debt of developing countries rose from $180 billion in 1975 to $406 billion in 1979. These loans were dollar denominated and had variable interest rates.

In 1978-1979, OPEC again cut oil supplies. This proved disastrous for developing nations. First of all, oil prices again rose, which meant that developing nations had to pay more to import oil, which meant that they could not industrialize as rapidly. Second, there was “a huge increase in interest rates caused by the industrialized countries’ economic stabilization policies.” When developed countries increased interest rates, it had several effects. Since loans were set at variable rates, these rates rose, and the amount that developing nations had to pay back increased. Also, when interest rates rose, the dollar appreciated, meaning that, in real terms, the loans to developing nations were worth more. Developing nations’ exports, which were the only means they had of paying back the loans, were still decreasing, and their growth was slowing because the price of oil was increasing. As they had more and more trouble paying back loans, developing nations took a final blow in the form of capital flight. Investors began to get nervous in the stability of their investments, and moved their capital to more secure locations. According to Todaro, “between 1976 and 1985, about $200 billion fled the heavily indebted countries. This was equivalent to 50% of the total borrowings by LDCs over the same period.”

These factors left many developing nations in a desperate situation. They had two options: either cut imports and impose contractionary fiscal and monetary policies, which would decrease growth further, or borrow more to pay back the existing debt. They

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52 Todaro, p. 554
53 Todaro, p. 555
initially chose the latter option, but this only worsened their debt. Eventually, they could no longer borrow from the financial sector, and had to seek aid from the IMF. The IMF would only grant loans upon certain conditions. These conditions became known as Structural Adjustment Policies, or SAPs. There are several features common to SAPs:\footnote{55}

1. Liberalizing foreign exchange and import controls
2. Devaluing the exchange rate
3. An anti-inflation program, usually consisting of decreased government spending, especially in social services and food subsidies, controlling wage increases, getting rid of price controls, and freeing the market
4. Increased foreign direct investment (FDI)

In the neoclassical model, SAPs are the avenue to Pareto Efficiency. According to the World Bank, “the basic objectives of SAPs were to restore macroeconomic stability…to revive economic growth through increased resource mobilization and more efficient utilization of resources. Efficiency gains would be achieved through greater reliance on market forces and on the private sector, and, in most developing countries, by reducing the role of government as a whole.”\footnote{56} We can see here the belief mentioned above that the free market is, according to the first welfare theorem, Pareto Efficient. Accordingly, the neoclassical answer to developing nations' problems is “ ‘Getting the prices right’: eliminating market distortions and increasing competition in the domestic market.”\footnote{57} If this is done, then the economy will grow, and people will be better off. However, it is important to note that “SAPs only have a medium-term focus, and are not

\footnote{54} Todaro, p. 555
\footnote{55} Todaro, p. 557
intended to deal directly with more fundamental development priorities such as poverty alleviation, reducing unemployment, and human capital development.”

We see here the economist attempting to operate under pure positivism. He can tell a country what to do to allocate resources efficiently in order to grow, but issues such as poverty, employment, etc. are not of fundamental importance, nor can they be within the positive-normative distinction.

B. Uganda and Structural Adjustment

While the story above gives a general framework for the debt crisis, it leaves out many details, especially regarding internal factors which devastated developing nations’ economies. In many LDCs, there was a bad infrastructure and high political instability that hurt their ability to stabilize the economy. Many countries were ruled by dictators who would take loan money and use it to finance projects which would gain them immediate popularity but had little long-term value. In many cases, poor policies played as large or a larger role than external factors in the crisis for developing nations.

This was certainly true in Uganda. In the late 1970s, it was ruled by Idi Amin. His rule was marked by insulation and corruption. Amin expelled and seized the property of “50,000 Asians, who had been engaged in trade, industry, and various professions.” While he “claimed that the ‘common man’ was the beneficiary of this drastic act—which proved immensely popular—it was actually the army that emerged with the houses, cars, and businesses of the departing Asian minority. This expropriation of property proved disastrous for the already declining economy.” Amin also enforced his

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57 ibid., p. 492
58 ibid., p. 492
59 Todaro, p. 719
will brutally. It is estimated that, during his rule, almost 300,000 people were killed. In 1979, Amin was overthrown, and Milton Obote ascended to power. He was overthrown in 1985, and civil war followed until Yoweri Museveni came to power in 1986. He has remained in power since then, and has transformed the country. In 1987, Uganda negotiated a policy framework paper with the IMF and the World Bank. It then began implementing a structural adjustment program “designed to restore price stability and sustainable balance of payments, improve capacity utilization, rehabilitate infrastructure, restore producer incentives through proper price policies, and improve resource mobilization and allocation in the public sector.”

In many ways, Uganda has been a shining star for developing countries that have implemented SAPs. It has grown at an average of 6.5% per year between 1986 and 1998. Inflation has dropped from triple digits in the mid-1980s to 4.6% in 1998. The economy has stabilized and appears able to continue growth. These results can be traced back to SAPs, which have promoted the more efficient allocation of resources. However, Uganda also serves as a type of paradox. While growth has been the norm, “poverty has intensified among the poor. Economic growth has not been reciprocated by equitable distribution.” Uganda has gotten worse in several major social indicators since the implementation of SAPs. Life expectancy decreased from 48 years in 1980-1985 to 42 years in 1989-1994. Infant mortality increased from 116 deaths per 1000 births to 122 over the same period and the maternal death rate went from 300 deaths per 100,000

61 ibid.
63 ibid.
64 World Development Indicators. “Uganda Data Profile.”
births to 550.  According to the report just quoted, “all of these figures point to a lower standard of living amongst the poor, who failed to profit from government reforms.”

Why has this occurred? There are several reasons that can be traced directly back to the SAPs instituted by Uganda. First, there was a reduction in government expenditures on social services, including health care. The government “has reduced its subsidies so that patients pay half the cost of medical treatment, and this has increased the burden on the poor.” When structural adjustment was implemented, the government cut expenditures, devalued the currency, opened up the economy to international competition, and kept wage pressure controlled. Therefore, workers earned less in real terms because the currency devalued, but they could not get higher wages. Firms in Uganda were forced to compete in the international arena, and many could not keep up. The result has been that, while growth has occurred, it has occurred at the expense of the poorest sectors of the population. According to the United Nations Development Report, “The link between economic growth and human development has been weak, including the period 1986-1995 during which significant macro-economic gains were achieved.”

It is also helpful to note that, despite the recent growth, Uganda remains heavily indebted. While the debt has decreased, Uganda still owes $3.5 billion, which is roughly 60% of GDP, and outside financial support is still needed to implement any future reforms.

C. Where the Christian View Differs from the Pareto principle

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67 ibid., p. 4
68 ibid., p. 4
In looking at the debt crisis, specifically as it relates to Uganda, there are three main areas where I believe someone operating from a Christian framework would have made different decisions than the ones that were made. The first area applies to the debt crisis in general and has to do with the increase in interest rates of developed countries. Here we can see why it is necessary to distinguish between Pareto-efficiency on a national level and an international level. For the U.S., it made sense to increase rates, because this was the only way to control inflation and stabilize things quickly. However, the increase badly hurt developing nations and plunged them into the crisis. While the policy may have been Pareto-efficient for the U.S., it was not on an international level. A Christian might suggest a smaller increase or providing a mechanism for stabilizing the interest rates on the loans of LDCs. The point is, a Christian view should take into account the effects U.S. economic changes have on the poorest of the poor, and this was not done in the early 1980s.

Secondly, and more importantly, I want to discuss SAPs. The argument for SAPs is that, while they may hurt countries in the short run, they will benefit them in the long run. One may ask the question, however, of how long is the long run? For many LDCs, SAPs have not helped them eliminate debt, while they have contributed to increased unemployment, greater poverty, and increased unrest. In Uganda, debt remains a large problem, and many social indicators have gotten worse even though there has been consistent growth. So, even if the long-term benefits will eventually be felt, what about the literally hundreds of thousands who, in the meantime, have starved or died from illness? SAPs do not adequately address these issues, and the reason is inherent in the neoclassical model. If efficiency is the ultimate standard for judging an allocation of
resources, then ideas like poverty or rights or justice are pushed into the background. While they may be considered indirectly, they are not in the forefront of neoclassical thought. In the neoclassical world, the most efficient allocation of resources will produce the most growth, which is seen as the key to making life better. Nothing is said about distribution, nor can it be said because of the positive/normative distinction. Issues such as the justness of the process are not addressed, because emphasis is placed on the end result: is there efficient allocation and growth?

The Christian framework would approach the problem differently. It would recognize poverty and rights alongside of growth. Since there is no positive-normative distinction, it could work on areas of distribution to make sure the poor are helped. In Uganda, while economic reforms were necessary, they could have been implemented more gradually, which would not have overwhelmed the poor as much. Also, safety nets could have been introduced which would have given the poor something to fall back on as things worsened for them. A Christian framework would offer a more comprehensive approach to solving the problem, instead of focusing on efficiency and growth.

A final point has to do with the remaining debt. There has recently been a movement called Jubilee 2000 which argues that developed countries should forgive at least some of the debts of LDCs. The idea behind this is that since, in some ways, developed countries had a hand in causing the debt (see the effects of the increase in interest rates above), they should cancel it. This would allow LDCs to begin growing again, and enable them to refocus from repaying billions in debt to social concerns such as poverty and equality. From a neoclassical framework, this is ludicrous, as it would amount to a loss in billions for developed countries. No American economist could argue
for this without making some type of appeal to justice or morality, which the neoclassical model forbids. However, this can be done in the Christian framework, and a strong case can be made for it within this framework.

VII. Conclusion: Where Do We Go From Here?

A. Is the Pareto principle inherently evil?

While this question may seem like it is taking us in a different direction from the rest of the paper, the answer to it is crucial as we seek to determine whether a Christian can operate within the neoclassical framework. If the principle is not inherently evil, then it becomes like many other things in this world which were not bad to begin with but have been twisted and distorted by sin.

One way to go about answering the above question is to discuss whether the Pareto principle would have been acceptable pre-Fall. As mentioned above, a key Christian principle is stewardship. Man has been given control over parts of the world to act as stewards for God. If we assume that the Fall did not happen, what would be the consequences. First, man’s preferences would be ordered correctly. His natural state would be one in communion with God, and he would desire to act to glorify Him. Under this scenario, the Pareto principle would not be morally erred, because instead of being based on the preferences of fallen man, it would be based on the preferences of man in communion with God which were in accordance with God’s commands.

The issue could be raised that this would still be a wrong standard, because it makes man, not God, the source of preferences. However, this ignores the fact that man by nature is “a decision-making creature, responsible to God, who should thus have the
God made man a decision-maker, and He gave man both the opportunity and command to make decisions in creation. Man is responsible to God for these decisions, and if the Fall had not occurred, he would make decisions in line with God’s commands. Thus, in a world where there was no Fall, the Pareto principle would potentially be acceptable on moral grounds.

B. Other Issues

While the Pareto principle is not inherently evil, it has been twisted and has many problems associated with it. While the problem does not lie in including preferences in the analysis, it lies in the fact that they are absolutized so that they are the only things considered. As mentioned above, preferences play an important role in decision-making. This is a feature of reality. We must also realize that the fact that men are fallen can contribute to the desire to give preferences an important role in the analysis. Fallen men often choose according to their sinful preferences rather than according to what glorifies God. Any economic model that wishes to reflect reality must take this into account. The neoclassical model is helpful in describing reality, and the Christian can use it in this way. However it errs in absolutizing individual preferences as the standard for how someone is better off and making normative prescriptions from this standard.

A more fundamental error in the Pareto principle is the positive/normative distinction from which it flows. What would be the effects of dissolving the distinction? As we have seen above, the distinction is something of a farce. Economists make value judgments all the time, so the pretense to be totally objective is not necessary. Second, the distinction limits the range over which the economist talks about reality. It forces the economist to ignore issues of distribution, even though they are obviously important. It

72 Monsma, p.176
also pushes questions of rights, justice, poverty, or equality into the background, because these issues are inherently value-laden. Getting rid of the distinction would probably not cause much upheaval, because it exists in name only anyway. It would allow the economist to incorporate distribution questions or other normative issues into the analysis, making it more acceptable for the Christian.

A third way in which the Pareto principle could be improved is if it is expanded to cover the international sector. Too often, nations do that which is efficient for them, ignoring the effects their actions may have on countries around the world, especially poorer ones. As argued above and demonstrated in the case study, often what is efficient for one country is inefficient on an international level. As our world becomes increasingly globalized and integrated, this approach becomes increasingly outdated. While this may prove to be a difficult step involving many problems of information and coordination, it is one which should be explored.

The neoclassical model has many problems, but we must realize that it has many benefits as well. Over the past decades, countries such as the United States have reached unprecedented levels of growth, managing to maintain this growth while keeping inflation low. While our capitalistic system has been around for much longer than the neoclassical model, for the past six decades, most policymakers involved in economic policy have operated with the neoclassical framework in mind. Their recommendations have been useful for our economic system, and it would be hard to say that the neoclassical model has had nothing to do with the growth our economy has experienced. While most of this growth has been reserved for the West, and issues such as distribution, rights, or justice have not been adequately addressed, it would be impossible to say that
the model has been a complete failure. Many of the problems with it can be corrected, and we must realize that there will never be a perfect model which will describe the whole of reality accurately. Every model will have problems, and every recommendation stemming from that model will have problems, but this does not mean that neither the model nor the recommendations are not useful.

So, the answer to whether a Christian can operate from the neoclassical framework in general and the Pareto principle specifically is yes, but with some qualifications. First, we must recognize both the problems and the merits of the model. Second, we must realize that a Christian does not have to accept the model in its entirety in order to work with it. While not perfect, the neoclassical model is a useful tool for describing how the world works. The biggest problems come from absolutizing preferences and the positive normative distinction. The Christian can use the model while simultaneously realizing the problems and working to correct them. We must realize that the world is fallen and that every model will be fallible in some way, even one which claims to be totally Christian. What the Christian can do is push to correct problems with the current model while working with it, and this can be done because the model is useful for describing reality. In many cases, the best way to make corrections is to be involved. While not perfect, the neoclassical model is probably the best one we have as of right now. Although we should constantly be seeking for ways to improve and correct it, we both can and should do this while engaging it and taking advantage of the areas it gets right, realizing that we will never get it perfect until Christ returns.
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