

The economics basis of marketing*

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Forethoughts

In beginning a discussion of the economic thinking that has become common marketing thinking, it is important to distinguish that part of the marketing field concerned with managerial control of markets and that which is a science of markets. Marketing thus sits in a commercial exchange economy between producers and consumers, as well as between economics and managerial practices. If we understand how 'the market' operates as an alternative to state authority, then we can see what marketing is supposed to do before focusing down on how to do marketing. To do this it is better to investigate economics from beyond the confines of the typical marketing or introductory economics textbook.

Marketing, when seen at the macro level, is a process for maximizing society's overall satisfaction – of economic enrichment – from the consumption of scarce resources. When seen at the micro level it appears much more like a process for inter-firm competition that manipulates consumer preferences. Marketing operates in and on the *market*. Since the eighteenth century, this has meant the society-wide space (institution) in which prices communicate preferences to producers of goods

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and services – so, not any longer the public meeting-place of earlier times, but, in the neoclassical tradition, an abstract supra-individual equilibrium mechanism, which stands as the bold alternative to tradition and central planning.

The notion of a competitive market is attractive to liberal sensibilities, since it implies shared meanings and fairness, social interdependence, and equal human dignity in transactions, contracts and promises, as well as the sanctity of contractual obligations. It aligns with conservative thought in offering a self-regulating alternative to state authority. Yet, the marketplace is recognizably fraught with opportunities for fraudulent behaviour, as rational human beings compete independently of each other in society.

The philosophic origins of marketing are largely founded on the liberal neoclassical economic thinking that has dominated the academic economics profession since the middle of the twentieth century – Hayek and Friedman are notable representatives. J.K. Galbraith calls this the ‘central tradition’ (Galbraith, 1970). This modern liberal tradition has been concerned with tempering the neoclassical economic analysis and advocating government intervention to correct market imperfections and failures. There are reservations about laissez-faire policies, and the power of large corporations is recognized as working against the perfect market competition assumption. The social desirability and consumption of some commodities is recognized as part of society’s general well-being, even though private capitalists would not make a profit from their production. Externalities are recognized as the cause of divergent private costs and social costs. The solution for all of these market imperfections is government intervention in the economy, rather than any extreme or perfect laissez-faire.

Some economists don’t take marketing very seriously, and consider the research and theory development to be facile. We will see that this is an interesting stance to take, given the status of economics. Those who study market efficiency within the structure-conduct-performance (SCP) paradigm see little significance in the practice of marketing. Others are looking to marketing to provide explanations of real market behaviour. For example, a major role of marketing is to present buyers with rules for making choices¹ and connections between products, vendors and lifestyles, and with cases for adopting these rules in their consumption decisions.

The purpose of this chapter is not to make economics experts out of marketing students, but rather to highlight the key origins, understandings and assumptions upon which marketing thought is apparently supported. We will explore the important consumer theory and producer theory concepts that we think we are familiar with from our marketing principles textbooks and lectures. The historical perspective, well beyond the current crop of introductory textbooks, reveals some intriguing insights and quite a few issues. It may be that many marketing students – and their lecturers – are not at all clear about the diversity of approaches to explaining market behaviour. An understanding of classical, neoclassical, behavioural and institutional perspectives can raise insights that are not evident when a single perspective is (perhaps unwittingly) taken. It is widely believed that economics began with one of Adam Smith’s books published in 1776. Economics then progressed with the

¹ A choice requires the relinquishment of desirable alternatives.

work of Jevons and Menger in 1871, adding marginal utility in the founding of the Austrian School of thinking. For others, modern economics came about in Hicks' 1937 formalization of the modelling approach (the neoclassical synthesis). A rather more diligent inquiry reveals important developments dating from 1570 and 1660, and an historical exploration of ideas, people and circumstances, is both intriguing and revealing. 'History of economics' texts are plentiful and rewarding reading (Canterbury, 1987; Guillet De Monthoux, 1993; Hunt, 2002; Roll, 1992; Routh, 1989). In the context of marketing, we consider what are the important concepts, interpretations, issues, and what misconceptions and vagueness in use are evident, as well as what is the essential nature of marketing when seen from the economics point of view?

Why have certain central concepts (exchange, value, etc.) become so prominent in everyday talk? Why did 'consumer behaviour' develop as a parallel field of study along with managerial marketing? We look below the surface appearances to understand the consequences and implications of adopting certain ideas and assumptions as the basis for the logic of marketing. In doing so, we are concerned that there seems to be an over-dependence on a misleading, even incomplete, orthodoxy in our undergraduate (and much of our postgraduate) marketing education. We can summarize this by observing that for most students of marketing, the subject of economics is synonymous with neoclassical (general equilibrium) thinking, and with the central assumption that growth is good (more is better). The mantra of 'marketing principles' is (almost entirely without reflection), 'wealth creation through competition and choice'.

As we will see, there is so much strong criticism and opposition to neoclassical economic thinking, that it seems prudent to disregard it as a satisfactory basis for understanding twenty-first-century marketing. Whereas Adam Smith is held up as the hero and founder of economics, and thus as a guide to the market and market control (marketing), that version of economics might be best disregarded. How can this be?

Economics

This discussion is about economy, and the field that studies human activity in the dynamic (changing) markets of economies is economics. Although 'the market' is rarely studied by marketing specialists, it is the *raison d'être* of the practices of marketing, and of the logic of economics, or rather marketing is the managerial technology for ensuring that the 'perfect' market isn't allowed to operate. The proactive form of managed marketing distorts the market for its own interests. Pretty much all of the economic theory that underlies orthodox marketing theory (Jones and Monieson, 1990) is of a neoclassical market model² that is widely adopted as a guide to practice. This is a problem because the model is largely a rhetorical tool. It purports to be descriptive, but only of an abstract theoretical institution, and

² For the typical economist, a 'model' is a small system of equations to describe some or all of an entire economy in terms of a few aggregative variables, often without recourse to actual data.

presents difficulties when applied to practical business problems, and, worse, it is also used prescriptively on that basis. Further, it doesn't represent actual market behaviour very well at all (Carrier, 1997)! The model is a simplification of a complex whole, yet it is common for people to simplistically invoke the 'laws of the market' in planning to persuade people to think and act in certain ways. The neoclassical economics framework is useful within limits, given its extreme assumptions about human behaviour, social structure and the nature of the biosphere (Ekins and Max-Neef, 1992; Stokes, 1992), yet is used well beyond situations for which the assumptions can be held valid.

In Western/Northern states, societies are market-directed as the primary basis for economic choices. That is the most convenient way of organizing economic aspects of life, especially when markets are not dominated by a few large corporations. The market logic has become firmly embedded in the modern mind, in both the private and public spheres, although most of us are peripherally aware that centrally planned (authoritative) and tradition-directed (historically determined) economies have existed and do operate, even as the market mechanism predominates. Citizens of democratic societies tend to equate market choice with freedom (or liberty, both narrowly defined) and the right to be individuals.

The dominant capitalist *provisioning system* (taking Applbbaum's (2004) extension beyond mere exchange and sales) is the shared, sometimes co-operative, process in which producers and consumers act to satisfy needs through the production and distribution of objects and the enactment of services. In this, the market, and therefore marketing, are central ideas. This capitalism, as we now understand it, has certain institutional and behavioural arrangements (Hunt, 2002): market-oriented commodity production; privately owned means of production; a majority of the population earning buying power by selling labour in the employment market; and ruggedly individualistic, acquisitive, utility-maximizing private enterprise behaviour by most individuals. The products have physical features that make them useable – they have use value. Further, they are valued because they can be sold for money in the market – they have exchange value. There is no direct connection between a person's productive capacity (to work) and their consumption, so exchange in the market mediates. Further, a person has no direct relationship with the producers of what they consume. Again, the market is a mediator since there is physical and psychological distance of producers from consumers.

In a social economy, where the maker of economic goods does not use them and the provider of economic services does not benefit from them, there is a real separation between producers and consumers. But while they are separated, they are also necessarily related. Hence, the separation is accompanied by an interdependence which is very real ... There is a natural, necessary attraction between the parties. Another name for this real, interdependent relationship between producer and consumer is a market. The market is the gap which separates producer and consumer. As the separation of producer and consumer grows greater under an expanding division of labor and increasingly differentiated consumer wants, the relationship becomes no less real but only more complex. (McInnes, 1964: 56)

Economics can be thought of as a 'derived' normative 'social science' that deals with what ought to be done to organize for economic tasks that maximize accomplished objectives (ends) with the allocation of scarce resources (means) through decision-making processes. Although economists have long strived to claim economics as a science, it is not now, and never has been, value-free. Robert Clower recalled that Swedish economist Johan Wicksell once said that it should not be the job of economists to make the commonsense difficult (Colander and Coats, 1989: 26).

Economics is limited (inexact) as a science because it is simplified and abstracted. Salient properties are selected from the multitude of variables that bear on the complex real-world economy, in intellectual experiments in the laboratory of the imagination, for the purpose of problem solving. It is thus an endeavour for understanding problems, as well as providing a basic language, and a common metaphor in 'the market'. It has provided concepts (tenets) for the marketing discipline, so we trace the sources of the foundational economic theories. In so doing, we get a picture of the current status, and a look towards the future of marketing. The dominant paradigm that persists was established in the seventeenth century during the Scientific Revolution and prior to the Industrial Revolution. Marketing's quest for scientific status is rather shakily, in the minds of many, built on the presumption that economics is an established science, although this is seemingly wrong!

The basic concepts of economics are a price economy, household and individual decision-making units, competitive business firms, a system of competitive pricing, and economic power to interfere with (manipulate) the supply-demand-price adjustment process. The market system produces order out of the decentralized decision making of buyers and consumers, reconciling many conflicting interests, and solving the problems of economic choice. The complex social and economic relationships of the market appears to each person as just so many impersonal relationships among things, and each person depends on the impersonal forces of buying (demand) and selling (supply) for the satisfaction of their needs.

Fundamental to the idea of the market, modern social conventions and pervading attitudes see the market as the source of satisfaction of subjectively recognized needs and of happiness, if only one can buy more things. This 'more is better' thinking is right to a point, yet extensive research shows that once a threshold of wealth is achieved, then diminishing returns set in and the more one gets the more needy one feels (see, e.g. various discussions of consumerism (De Graaf et al., 2002; Hamilton and Denniss, 2005; James, 2006, 2007; Lane, 2000, 1991)). Economic growth isn't necessarily creating high levels of life satisfaction, genuine well-being and true happiness for society (Myers, 2000; Speth, 2008).

We can think of economics as the social 'science' that analyses decisions about the allocation of scarce resources among alternative uses by individuals, companies and states to satisfy wants – what to produce, how to produce, and how to distribute to society, and the consumption of exchangeable personal property ('goods³ and services'). This is mostly about how markets are organized, participants and

³ What is the origin of referring to exchangeable objects as 'goods', given that this sounds like a generally applicable positive evaluation?

their behaviour, and the effects of patterns of behaviour on social welfare. Marketers are interested in the (assumed) rationality of buying behaviour, which is the behaviour of individuals in markets when faced with a choice. The challenge is to understand why people behave as they do in economic situations. If marketing is the answer, what (from an economics point of view) are the questions? How does the market operate? How do decision-making units behave in and out of the market?

Whereas micro-analysis deals with how individual buyers interact through the market with sellers in terms of prices, income, preferences, and so on, macro-analysis attends to the economy as a whole. Micro-economics has a role in relation to management that is akin to the role that macro-economics plays in politics (Kay, 1996). Importantly, we should note the distinction between thinking of a society as an economy and thinking of a society as having an economy, and understand economy as an autonomous sphere of trading activity that impresses rules on everything else. Increasingly, society is governed by the rules of the market as the commercial ethos takes root (see for example, *In Praise of Commercial Culture* (Cowen, 1998)). 'The whole society is in one sense part of the economy, in that all of its units, individual and collective, participate in the economy. Thus households, universities, hospitals, units of government, churches etc. are in the economy. But no concrete unit is "purely economic"' (Parsons and Smelser, 1956: 14).

Knowledge of marketing in a range of fields attempts to understand human organization and behaviour and modification for human ends. In this multitude of perspectives, economics seems to be the natural integrative discipline of management science. Significantly, it explains, but also influences market behaviour.

All societies produce, distribute and consume things. It is only in modern societies that such 'goods' and their prices, and the conditions of ownership and work, are determined by 'laws' of economic efficiency (note, not equality) in pursuit of material wealth accumulation (Sachs, 1992).

Sociology examines the internal structure of marketing groups and their interaction, whilst *political science* considers legislation, regulation, and the judiciary that determine market structure and behaviour. *Psychology* studies manifestations of personal behaviour in market activity, examining unobservable attitudes, learning, motivation and personality to explain the observable behaviour. *Social psychology*, on the other hand, examines marketing activities as the behaviour of socialized individuals. *Anthropology* is concerned with physical, social and cultural origins of market relationships. Importantly, these perspectives deal with understanding relations of meaning rather than explaining cause and effect relations. The *ecology* perspective seeks to understand the relationship of market participants and their environment.

Although marketing is usually learned as a managerial technology, it has considerable scope beyond. Indeed 12 schools of thought covering economic and non-economic purposes, and interactive and non-interactive forms, of which managerial marketing is just one possibility, can be discerned (Sheth et al., 1988).

Economics is the study of market organization and the behaviour and interaction of producers and consumers, and the effects on resource use and allocation. The subject is people contemplating the money they earn and the money they need for consumption (Galbraith and Salinger, 1978). This perspective presupposes the

dominance of an economic enrichment motive, and the natural environment as a set of resources for this purpose.

The economic, social and ethical are inextricably intertwined – any ‘pure’ economics is simplified and abstracted from reality and is of limited use. The world cannot be represented completely from a single point of view, nor intelligibly if represented with all! The non-economic – moral, social and political – are important aspects of our lives, so it is better to view from many points of view sequentially, thus being aware of particular prejudices of specific views.

In considering the economics basis for marketing, we are interested in appreciating what we need to understand in economics in order to understand marketing’s purpose and practices, so it is easy to think of marketing as just applied economics. Partly this involves the mastering of the language of economists, who are concerned with explaining and predicting the satisfaction of wants through the supply of industrial and consumer goods and services and the achievement of economic exchange relationships played out in the buying and selling activities in which assets are exchanged by two parties, each motivated by the desire for gain.

Economics emerged at the end of the nineteenth century out of the political economy⁴ of Adam Smith and later early thinkers, just as the discipline of marketing was also emerging formally. This narrowed the field of inquiry, assuming that government was outside the market in which producers and consumers came together. All important needs would be supplied by the market, the all-powerful regulatory force in society. Galbraith observes that economics was political economy ‘cleansed of politics’ (Galbraith and Salinger, 1978: 5). As we will see later in this discussion, some economists these days are arguing for a return to political economy.

Marketing is an economic activity, for sure, but it is important to recognize that economic tools can be used to accomplish economic as well as other objectives. Further, knowledge beyond economics may be required for the effective use of economic resources. This highlights the social nature of marketing (Douglas, 1975). Indeed, well before the emergence of relationship marketing, the scope of marketing was recognized. Bartels proposed two ways to understand marketing, as a managerial technology, and as a social process. As a technology of things, marketing is an impersonal act for the achievement of self-determined corporate goals, drawing on economic concepts, space–time, processes, intangibles, objects. Alternatively, marketing is a process of social interaction, a system of role relationships, and a type of management responsibility. In this view, the process of marketing is social, in which society fulfils personal and institutional needs for goods and services, in the action and interaction of *people*. Thus, marketing is understood as the sets of relationships which arise in the performance of the process of economic want-satisfaction, and is behaviour in relationships (Bartels, 1970). This highlights the co-ordinating function of the discipline of marketing, as a social system for organizing.

⁴ This name was current before it became fashionable to treat economics as a science, then for the purpose of gaining respectability. Clearly it is not, since the economist’s subject ‘is flooded by the human powers of discovery and imagination’ (Shackle, 1973: 122). In other words, the market, in this view, is not a ‘mechanism’, since individual action is subjective.

The evolution of economics and the adoption of neoclassical thought

Economics provides analytical tools for the interpretation of recorded history. Facts never tell their own story, so theorizing is necessary in applying the humanities and sciences in the political economy of life. Logical reasoning is fundamental in making all economics useful in describing, analysing and explaining, and at the higher levels of economic theory, mathematics is also necessary for modelling and correlation in a systematic pattern. So what did the emerging field of economics assume about the individual and their fate in a commercial society?

Economics has its Western foundations in the thinking of a number of important figures who have contributed to the discipline leading up to and during the eighteenth-century Scottish Enlightenment, in the outpouring of the assertion of reason above authority, and the 'science of man'. Most of these people were British (and men). Then, during the birth of the discipline of marketing at the beginning of the twentieth century, the men who established the first university departments in the United States of America had mostly studied in the Austrian School.⁵ Their perspective emphasizes the spontaneous organizing power of the price mechanism, holds that the complexity of subjective human choices makes mathematical modelling of the evolving market extremely difficult (or impossible) and therefore advocates a laissez-faire approach to the economy – focusing on the entrepreneur as the matcher of capabilities and wants. They are the founding figures who influenced early foundational marketing thinking. Economists' ideas cannot be dissociated from their personal situations and the prevailing social conditions of their time, and so a historical perspective is important. The early economists mostly had little influence during their lifetimes and not until several generations later did their thinking impact on ideas about social betterment, now deeply embedded in the institutions we live by, including our notions of social justice. These people made the history – they shaped our modern minds on what we still regard as the idea of market economy.

Critique of mainstream 'neoclassical marketing': the economic functions of markets and marketing

Economics is the study of how people and society end up choosing, with or without the use of money, to employ scarce productive resources that could have alternative uses, to produce various commodities and distribute them for consumption, now or in the future, among various persons and groups in society. It analyzes the costs and benefits of improving patterns of resource allocation. (Samuelson, 1976: 3)

⁵ The Austrian School emphasizes the market as a discovery process, naturally and spontaneously evolving out of human interdependence and interaction. (see, e.g. Hayek, 1978).

There is a rich tradition around the birth of formalized marketing in the early 1900s. Some would argue that marketing emerged as a sub-discipline of economics, whilst others would suggest that marketing is a branch of applied economics, with its origins in economics as a foundation, plus a strong emphasis on the seller's viewpoint. Marketing has evolved considerably, taking in non-economic explanations of seller and buyer behaviour, and increasingly emphasizing the viewpoint of the buyer (Sheth et al., 1988). Marketing has had a highly focused, but rather narrow, explanation of marketplace behaviour, assuming economic values as drivers of actor behaviour. The purpose of the marketing system is seen as the fulfilment of individual consumer needs, seeking efficiency in their actions to maximize profits. Critical economic variables are production and distribution efficiency, prices and outputs, and consumer income levels. The underlying condition is the use of finite incomes to satisfy unlimited wants. Non-economic factors would be the domain of the psychologist, sociologist and anthropologist, and would increasingly come into marketing thinking in the twentieth century. The economic perspective applies certain values, orientation, and 'basic' philosophies to the problem of market operation.

Orthodox economists see the market automatically adjusting supply and demand. Heterodox economists (e.g. Williamson, 1985) and sociologists (e.g. Herbert Simon) see managerial practices shaping the market, and see choice objectives other than utility maximization. Thus, in this view, marketing *performs* the market, it doesn't just react to it. Interestingly, it can be observed that whilst economics has been the inspiring discipline for marketing, it has not directly provided useful frameworks (Cochoy, 1998).

Political economy, or the classical school, originated in moral philosophy and came to be the study of production and buying and selling, in relation to custom, law and government. This field flourished from about 1700 to almost the end of the nineteenth century, just prior to the establishment of the institution of marketing in the early twentieth century. Reference to the *Oxford English Dictionary*, however, shows that a system of provisioning had been developing since the sixteenth century, long before a marketing discipline was formalized (in theory or in practice).

By about 1870, the term 'economics' had been adopted for the neoclassical school of thought, following Alfred Marshall. Whereas the classical school studied factors of long-run growth and change in the then emerging capitalist economy, the neoclassical focus was on the way that resources are allocated to meet the wants of the population of the state. The market was seen as the mechanism that could harmoniously reconcile the differing interests of producer and consumer and of employees and employers. A market model and theory of individual choice were developed to explain individual decision making towards profit maximization by the firm, and utility (happiness) maximization by each individual consumer. Economics became the study of market actor behaviour and material decisions.

It is vital to realize that the market is not what people do and think, and how they interact when they buy and sell, give and take. It is a conception of an idealized form of buying and selling – a culturally-determined construct, an idea of a sphere of life. The evolving marketing logic largely adopted the early economists' constructions of market system and market actors.

The market model is a representation of a mechanism for generating personal sustenance and prosperity (looking to the future). It was considered natural (as evolving) – what people would do spontaneously if not constrained. Economies exist because people trade, and not the other way around. Thus, wealth was created because of the division of labour through the increased efficiency of specialization and consequent technical progress. This mechanism was capable of producing greater utility and satisfaction than by other means, through efficiency in resource allocation. Thus a rational motor for growth was identified that could provide the greatest net human welfare.

In adopting neoclassical thinking, a number of significant *assumptions* are made about people and their conditions, with departures from the ideal having been considered sinful or negligent or incompetent, such has been the power of this rationality. These theories to which undergraduates are subjected instil misconceptions, and it is helpful to recognize that the orthodox market model is too unrealistic to be generally acceptable, yet, this is just how it is passed on, as established ‘common knowledge’. We will now reflect on some key assumptions that make the model unlike anything real.

Firstly, choice is taken, axiomatically, to be the *essence* of the economy. In ‘economic choice-making’ it is most rational to maximize utility, but the model did not account for individual behaviour but rather the average behaviour of a system of the economy. In this view, we live in an atomistic world of individuals, each with an individual identity and autonomy. Market actors are and must be autonomous, so the market is a means of communication between consumers and producers. This plays out secular, acquisitive individualism. The basic goal of the individual is to satisfy their own materialistic wants, in pursuit of self-centred, hedonistic tastes ordered in a pattern of desire, a pre-existing and unchanging set of preferences. In this economic (instrumental) rationality of marginality, we always want more for less. Because ends are infinite, in the rational calculating spirit of capitalism individuals choose the best action according to stable preference functions and the constraints facing them. This is a world of asocial buyers and sellers focused on self-interest in interaction, wielding dispassionate judgement in their calculation of gain, dealing with each other from a distance, in conflict because each wants more for less. There is displayed in this thinking a belief that the exchange process monitors individual values (‘laws of the market’ and ‘the invisible hand of the market’). This equates market prices and social values. In earlier thinking, a civilizing and pacifying influence and moralizing agency was ascribed to the market in the eighteenth century, in which exchange would create prosperity by dealing to mutual interests, thus inhibiting aggression.

Hirschman examines the notion of ‘interest’ and the rather narrow meaning that is adopted in marketing as the drive for material economic advantage. This motivation for rational instrumental action was assumed in the eighteenth century and is still regarded by some as a ‘law’ of human motivation, obviously preferable to ‘destructive passions’. Hirschman elaborates this view well, that interest is ‘the construct of the self-interested, isolated individual who chooses freely and rationally between alternative courses of action after computing their prospective costs and benefits to him or herself, that is while ignoring costs and benefits to other people

and to society at large' (Hirschman, 1986: 36). This is a person who is self-centred in 'minding their own business'. Since Adam Smith (1776), who saw growth as an inherent characteristic of capitalism, there has been a belief that the pursuit of private gain indirectly serves the public interest. The Scottish satirical writer, essayist, historian and social commentator, Thomas Carlyle (1795–1881), observed this shift from medieval values of glory and chivalry to the calculation of 'a profit and loss philosophy'. Some argue that commerce produces civilized society, whilst others see civilized society as the basis for commerce.

This world view further presumes that buyer choice is a moral good, entailing competition among sellers,⁶ who will thus innovate, extending choice and increasing efficiency. The producing firm is a 'black box', and people are selfish individuals who will act deviously if the price is right in one-off encounters around price. Enlightened self-interest is a sense of the necessity to 'give up something to not lose everything'.

All moral rights are taken to lie in the individual, who is the legitimate decision maker. Thus, 'consumer sovereignty' implies and accepts that attempts to modify tastes are inappropriate. The market comprises many price-taking anonymous buyers and many sellers supplied with perfect information to support the most efficient decisions. This perfect competition is the regulator impersonally setting prices, and beyond the power of any individual. At the point of equilibrium, when supply and demand naturally balance, there appears to actors to be no other price deal that would improve their allocation of resource. This is a natural mechanism, and as such requires little government intervention to ensure 'free trade'.

The abstract modelling positivistic science of neoclassical economics provides a convenient simplified explanation of the world which is purely competitive, with perfect information, moving towards general equilibrium of supply and demand, in which buyers are indifferent to rival suppliers of identical product characteristics. Real-world ambiguities are assumed away in explaining society as a 'price system'. This was to be expected in the emergent modernism, which emphasizes the institutions of science (mechanistic causality), state (bureaucratic rationality) and market (law of supply and demand). This is, of course, a limited culture-specific logic, not generally applicable as it appears.

The neoclassical synthesis approach as we now know it was developed in the 1930s (Hicks, 1946; Hicks and Allen, 1934). It is *deductive*, in that axioms are assembled to build rigorous models of consumer behaviour, each with its own simplifying assumptions: well-defined preferences and constraints, equilibrium states, constrained optimization. In this paradigm, it is presumed that we 'know' that demand, supply and price are co-determined and tend to equilibrium. It is assumed that all that is necessary to be known is known. This global rationality comes about because of the bounded rationality of the neoclassical economist. For past decades, economists have had a predilection for deductive reasoning, rather than empirical investigation (Eichner, 1983).

⁶ Adam Smith observed many small firms in increasingly intense competition as the Industrial Revolution emerged in England, following the Scientific Revolution in Europe. Much of his thinking is still applied today, even though we experience quite different circumstances, and his assumptions, drawn from his religious beliefs and naive natural science, no longer fit.

In Routh's view, the standard economics textbooks (especially those of Samuelson and Lipsey) are 'powerful instruments of disorientation; for confusing the mind and preparing it for the acceptance of myths of growing complexity and unreality' (Routh, 1989: 339). Notable exceptions are Robinson and Eatwell (1973), Koutsoyiannis (1975) and Heilbroner and Thurow (1982).

The 'economistic fallacy' identifies the abstract model with reality, thus considering real behaviour only to the extent that it corresponds to the model, and moving to policy conclusions from a highly abstract basis. It universalizes the nature of the economic activity of a particular place and time, and assumes that as the essence of economic activity at all times and places (it is radically ethnocentric). The economics focus is economizing behaviour that pursues optimal resource allocation. Alternative 'heterodox' approaches, however, study the ways in which different societies provide for their material needs, and the various ways in which they solve their economic problem. The *institutionalist* approach, thus, is concerned with social rather than market values (Stanfield, 1983).

Heterodox analysis does not assume full rationality – psychological factors are accounted for. By the 1950s, a more *inductive* approach was developing, in which actual decision making problems were examined to generate generally applicable theory (Simon, 1957, 1959). In this view, choice is an ongoing problem-solving process during which consumer viewpoints, aspirations, habits, beliefs and wants evolve through a decision cycle. A burgeoning consumer behaviour field has been developed on this basis (Blackwell et al. 1969, 2005). Herbert Simon argued that all decisions are made within bounded rationality: 'The capacity of the human mind for formulating and solving complex problems is very small compared to the size of the problems whose solution is required for objectively rational behavior in the real world' (1957: 198). The market model simply was too simple! *Behavioural* economics integrates insights from neoclassical economics and psychology to take account of cognitive and emotional factors in better understanding economic decisions, thus challenging assumptions of rational behaviour. Importantly, Adam Smith (1776) had described psychological aspects of individual behaviour, and Jeremy Bentham's work on utility (1793) considered psychological factors extensively. Gary Becker's economic *theory of crime* (1968) is considered a seminal work on psychological elements of economic decision making.

By the 1980s, marketers and economists had differing perspectives! Whereas the neoclassical perspective saw selling costs as wasteful and pernicious, and product differentiation as no more than trickery, marketers had qualifying assumptions within the emerging thinking about the firm's competitive strategies (Earle, 1995).

The operation of the economy and behaviour of its actors can best be understood as part of the wider reality. The simplified modelling removes the extensive richness of non-equilibrium conditions. For example, much of the controversy over perfect and imperfect competition analysis of pricing behaviour and supply and demand theory seems to have passed by the world of the marketing student and their lecturers. As early as the 1950s, imperfect competition became the normal assumption (Chamberlin, 1933; Robinson, 1933, 1953). It is also revealing to note that, among others, Nicholas Kaldor, a market equilibrium fan in 1934, then thought it irrelevant by 1972 (Kaldor, 1934, 1972). Also, notable is Hicks' 1979 comment: 'As

economics pushes on beyond “statics”, it becomes less like science and more like history’ (Hicks, 1979: xi). Other critics have seen that a static equilibrium never can, and never should, exist, and regarded the continuing belief in this idea as a ‘major ill’ in (especially American) economics. The mechanistic view cannot deal adequately with the dynamic, interactive complexity of society.

Given the assumptions outlined earlier, it remains to be asked whether the market mechanism as the basis for society produces social integration (Durkheim, 1964 [1893]; Simmel, 1955 [1922]) or corrosive atomism (Horkheimer, 1974; Schumpeter, 1954)? The assumption of autonomous individuals each with a freely-chosen different identity denies sociality, morality and cultural values. Bagozzi has recently propounded a corrective (Bagozzi, 2005), because the neoclassical *homo economicus* does not account for altruism, commitment to ethical values, concern for the group and the public interest, and a variety of non-instrumental behaviour.

Heterogeneity of interests is assumed away, and reasons for desires are considered irrelevant in that world of ‘if you want it, you can have it all – if you can pay for it’. Rationality assumes that each individual can foresee the consequences of their actions and the actions of others, as well as everyone’s abilities and intentions. Yet, in practice there are highly significant information imperfections. There is ignorance and incomplete information on both the supply side and among buyers (actual and potential customers).

In theory, of the neoclassical kind, sovereign consumers influence what should be produced through continuing marginal adjustments. But this is not how consumers really behave. The information needed to construct a market demand curve, which purports to show what demand would be at various prices, is never known before the fact of actual market outcomes. Such a simple analysis also assumes that expectations are realized. This raises another issue with the role of utility. This is an abstract concept denoting subjective pleasure, usefulness, or derived satisfaction. But in market activity, consumers may also be disappointed in their expectations. They may also be cheated, misled, or otherwise suffer, resulting in remorse instead of enjoyment of utility.

Nor does the market model very accurately represent the actual behaviour of firms – it is common that firms that deal with each other over an extended period seek stability in the face of uncertainty (the future and the behaviour of others), and establish relatively durable relations with a clear moral aspect. These marketing relationships are regulated by criteria of fairness and strong expectations of trust and abstention from opportunism. These firms abandon autonomy and competition for the possibility of certainty. There is a considerable recent literature on marketing relationships and so-called ‘contracting’ (see Block, 1990; Dore, 1983; Foxall, 1999; Granovetter, 1985; Macauley, 1963).

Nor is competition perfect in that the reality is an oligopoly. There is a concentration of market power (to set prices and other terms) when there are a few large corporations (20 per cent of marketers win 80 per cent of the business), then the market model mechanism will not operate as an impersonal competitive market. Each powerful actor has market power to set prices for itself. Even without this problem, there are logical difficulties with the notion of a supply curve – who sets the price if all producers are price-takers? (Arrow, 1959).

Other issues that make the market model untenable include: the prevalence of non-price aspects of competition; the interdependence of cost and revenue functions; the dynamic changing nature of the market; innovation and new product launch ('creative destruction') in which buyer and seller both learn (Schumpeter, 1991); competitors who respond to market devices (dynamic competition); uneven distribution of power among sellers and buyers; and identical product offerings that do not lead to pro-rata market share. Because the 'no information problem' assumption is invalid, and consumers do not choose randomly among identical offers, increased goodwill leads to increased market share, and word-of-mouth effects and trust-based relationships are effective.

Nor does the model account for moral commitments. It is easily observed that our normative and affective values and emotions heavily influence our choices. Social groups and communities are often the context for decisions, and normative rules apply for commitment to fairness in competition and trust that this is the commitment of others. Social bonds reflect the reality that competition thrives in social communities where they are strong enough to sustain 'natural' trust and low transaction costs, but not so strong as to suppress exchange. This is not so in impersonal calculative systems of independent actors unbounded by social relations. It is important to understand that firms exist to modify market relationships by introducing mutuality, thereby turning them into marketing relationships (Foxall, 1999). The neoclassical paradigm under-emphasizes the significance of ethical judgements in accounting for market behaviour and policy making.

For example, economist Gary Becker appears to treat children as 'durable consumer goods' that can be traded-off for other goods (a new car, for example) (Becker, 1976). This calculative mentality debases moral values, secularizing cost-benefit calculations in the otherwise sacred, for example legitimizing the selling of rights to pollute.

Finally, the term 'free market' imputes a pejorative feel to the notion of government intervention, yet there are no examples of workable intervention-free economies.

It is peculiar that only one view of economics is adopted, especially since that is invariably neoclassical economics with its limited practical application! This way of thinking is ill-suited to framing business and public-policy problems. Perhaps this is all that textbook authors were taught in business school. This approach circumscribes the possibilities of recognizing the implications of this particular way of thinking.

Then again, why should we expect a way of thinking that was crafted before the dawn of large corporations and our age of affluence, that we now take for granted – especially the Generation X – to remain eternally relevant and helpful? We still expect the economic basis of marketing to be the neoclassical (equilibrium market) logic, but it should by now be behavioural (consumer choice) and institutional (firms) economics to which we turn for analytical support of our problem-solving – to understand people in pursuit of profit for a purpose. 'Betterment' was the term used by Adam Smith in the language of the eighteenth century, but see also Kenneth Boulding on *welfare* economics more recently (Boulding, 1984).

So what form of economic analysis is more useful for understanding and shaping the form and purpose of marketing? The 'invisible hand' of the market is a far too well entrenched idea, and even economists doubt its usefulness: 'Is it true that the

pursuit of private interests produces not chaos but coherence, and if so, how is it done?’ (Hahn, 1970: 1).

There has been extensive *reformation* of the market model. The *institutional* view extends the traditional view, by asking questions the neoclassical approach claimed not to address. For example, social institutions are considered as existing prior to, and thus conditioning, individual behaviour. Markets are considered to be the result of the complex interactions of a range of institutions with diverging interests. Key figures include Thorstein Veblen, John R. Commons (Commons, 1924, 1934), Adolf Berle (1895–1971) and John Kenneth Galbraith. Institutional analysis defines the economy differently, adopts a different method of inquiry, and applies alternative values in constructing meaning from its inquiry.

Transaction cost economics deals with the reality of a lack of knowledge and less than perfectly rational decision making (Williamson, 1975, 1985). However, it is important to realize that Williamson adheres to the neoclassical assumption that people are selfish individuals who will act deviously if the price is right – he considers only the opportunism scenario. Information economics deals with the lack of information, often asymmetric, and thus the inevitability of information costs, divergence of interests, and the firm as the nexus of contracts in various forms.

Markets are seen as partly mechanisms that facilitate contractual agreements and the exchange of property rights by supporting consensus on prices and communicating information about products, prices, quantities, potential buyers and potential sellers. Thus, the market can be defined as ‘a set of social institutions in which a large number of commodity exchanges of a specific type regularly take place, and to some extent are facilitated and structured by those institutions’ (Hodgson, 1988: 174).

Economic sociology focuses on how market exchange arises from social relations, shifting attention from exchange as events in pre-existing markets, to understanding markets as social institutions. It is argued that marketing brings about markets – marketing is a market-making activity (Araujo, 2007; Callon, 1998; Callon et al., 2007).

Reflections

We should be careful to not ask what economics is, but rather what it has been, how it got to be what it is now, and what it can be? It is a developing discipline, which corrects its mistakes and omissions. The value of a knowledge of economics to a prospective marketing executive is in understanding the market metaphor and thus the purpose of marketing. But there is a social responsibility to not limit understanding to ‘market’ and ‘exchange’ in the pursuit merely of how to do better marketing. It raises the possibility of answering what can marketing be and for what purpose?

Economics has always been focused on human action, with the goal of predicting and explaining the behaviour of people in social groups, as distinct from that of the individual. Yet, studies of ‘rational economic man’ are blind to social organization. As one of the humanities, economics inquiry can provide understanding, which in turn drives the very social system it studies. ‘Modern’ economists have formulated economic ‘laws’ as if they are immutable ‘laws of nature’, yet economics must deal with people.

It has to deal with the social and political if it is to be truly helpful outside the academic discipline (Canterbery, 1987). Too much modern economics supposes that people behave like inanimate particles in a clock-like mechanism. Microeconomic analysis explained decision making by individual buyers, who maximized satisfaction by choosing among assortments of goods and services, and individual sellers, whose manipulation of marketing variables contributed to social welfare. However, market behaviour could not be studied in isolation if the market is understood as a social institution. Macroeconomic thinking was necessary to an understanding of the interactions between the market and other social institutions (Dixon, 2002).

The study of marketing can be for the accumulation of market intelligence, but also for understanding the possibilities for social betterment. In this regard, we can ask whether scholars of marketing need to treat consumers like fish in the way that fishermen study them, or in the way that marine biologists study them? (Tuck, 1976).

It is hard to separate attitude to market form and function from political views. The market seems attractive from the marketing point of view. However, the market, according to the economist, controls income as well as spending power since most consumers are also earners. So, for the individual, the market is a discipline that many would prefer to escape. In returning to the political economy of the moral philosophers, it would seem that rehumanizing our provisioning needs is a reorientation to a greater focus on people and a lesser emphasis on things. A balance of natural, economic and social systems for sufficiency in a resource-light economy focuses on whether less emphasis on economic expansion can enhance the quality of civilization by asking 'how much is enough?' (Diener and Seligman, 2004; Durning, 1992).

The blindness of the market to any claim on society's output except wealth and income creates very serious problems (Heilbroner and Thurow, 1982). In redefining wealth we might observe that the 'faster, further, more' mentality may be counter-productive. Even as wants (ends) seem infinite and mostly unmet, creating a sense of scarcity of means, there is a simultaneous assumption of abundance of sources and sinks for the production and waste of material output that is to supply satisfactions, and thus presumed to be the source of wealth and well-being. This presumption, since the nineteenth century, of continuously expanding wants, of course renders any and all means insufficient. Well-being has been understood as 'well-having', that welfare depends on material output. Production growth has been taken for granted, so the solution to resource limits has been to improve efficiency of means.

In conditions of abundance, product utility is taken for granted, so experiences and identity, that is, the symbolic value of goods and services, becomes paramount. By labelling nature as 'resource', as useful inputs to industry, we have removed limits on exploitation. In industrial society's consumption of nature – by producers, and thus consumers – we have become 'cheerful enemies of nature' (Sachs, 1999) in our ever-expanding commodification.

The problem facing economics today is not the efficient allocation of resources, but how society should live, or what, how much and in what way it should produce and consume – this focuses on values and institutional patterns (qualities) rather than energy-material processes (quantities). Indeed, lower levels of production may enhance well-being. Opportunities abound in the search for a society that is able to not want what it would be capable of providing. Self-restraint and intermediate performance, within forms of prosperity that don't require permanent growth, will

require a suitable form of marketing: 'the productivity of a sustainable society will be measured not by the eco-efficiency of an ever expanding number of technologies, but by the quality of the civilization it creates out of limited means' (Sachs, 1999: 182).

So, my final thought is what if the economics basis of marketing was less tautological, more empirical, and non-axiomatic and non-atomistic? Typical teaching does not recognize the effects of the loss of historical connections in the field of economics. The problem addressed in the neoclassical foundation, especially in the basic maximizing model, is not of the real world of actual buyers and sellers interacting, but of the abstracted models in the mental operations of theorists. Much of the work is the outcrop of a mere fascination with the problems of optimal resource allocation, and many of the key propositions cannot be empirically demonstrated. The 'introductory principles of economics' are useful as a beginner's tool kit, but are grossly over-extended when applied to real management problems. Neoclassical economics, especially of the mathematical formalist, aims to explain all of reality without even looking at it (Mini, 1974). There is little real relevance to everyday life!

In accepting, even seeking, an economic basis for marketing, we need to also deal with the problems of adopting, uncritically, the orthodoxy. There remain serious concerns about assuming a stable, stationary equilibrium as the foundation for marketing principles. The resulting convenient analyses are practically meaningless, and worse, misleading. What of a marketing that has a more realistic basis? This is already the case, well beyond the 'useful myth' of the 'self-regulating' market mechanism.

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