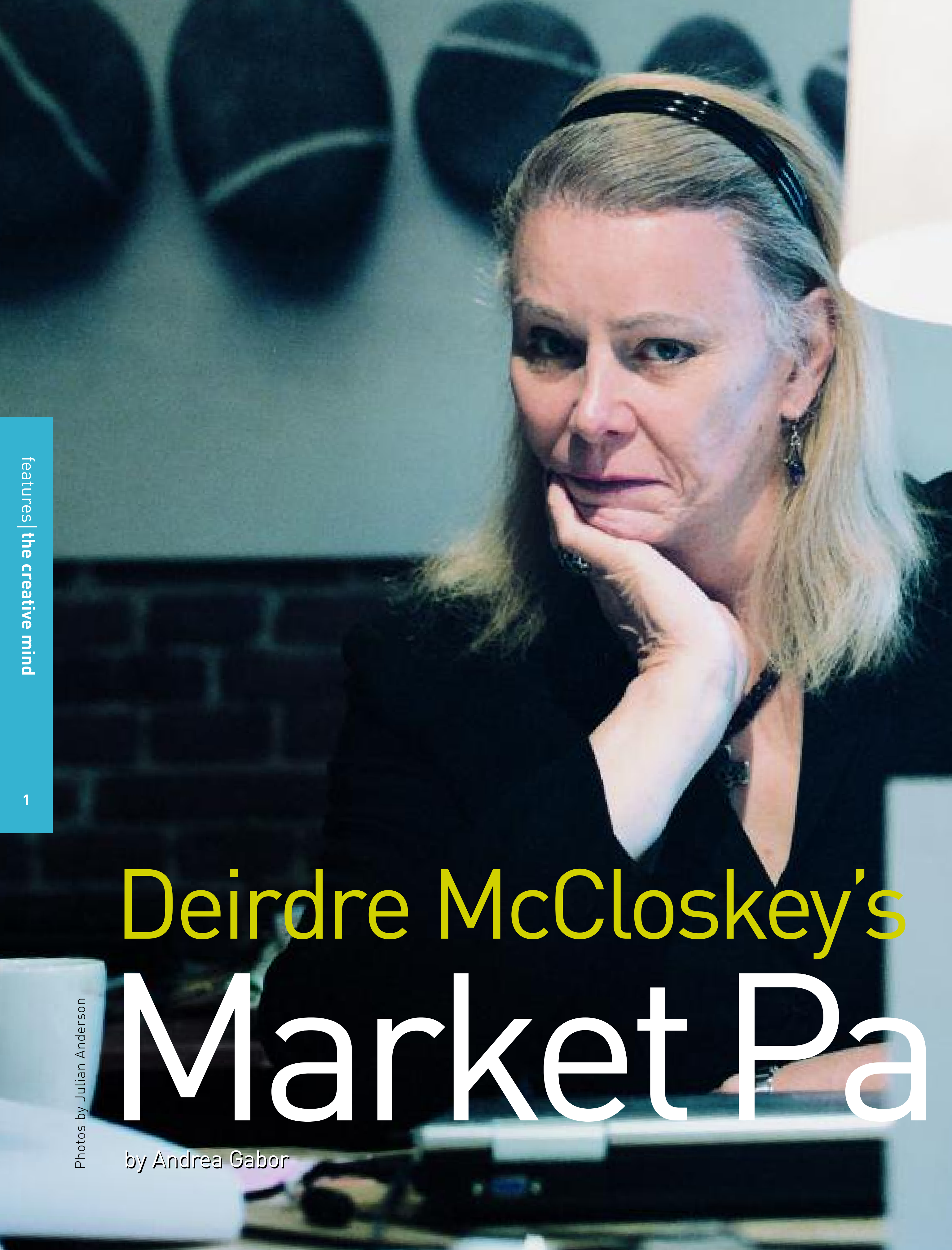

Photos by Julian Anderson

# Deirdre McCloskey's Market Pa

by Andrea Gabor

An idiosyncratic economist preaches the innate morality of business.

# th to Virtue

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(aagabor@aol.com) is the author of several books, including *The Capitalist Philosophers: The Geniuses of Modern Business — Their Lives, Times, and Ideas* (Three Rivers Press, 2002). She is a professor of business journalism at Baruch College/CUNY.





**Economists are famously abstract: They seem to** prefer to examine the world through the lens of elegant mathematical models. But Deirdre McCloskey, a professor of economics, English, and history at the University of Illinois at Chicago, has become one of the most prominent and unorthodox voices in her field by attacking that tendency head-on. She routinely questions the discipline's most fundamental assumptions.

Now she is raising the stakes with a wholesale challenge to her profession, one that questions long-held interpretations of laissez-faire economics. Her new book, *The Bourgeois Virtues: Ethics for an Age of Commerce* (University of Chicago Press, 2006), is the first in a planned four-volume apologia of capitalism. Rather than laying out the standard defense of free markets, Professor McCloskey's work, an ambitious survey of the history of capitalism from Plato to social critic Barbara Ehrenreich, argues that it is a far more ethical system than either its advocates or its disparagers recognize. The hoary contention that capitalism is based solely on utilitarian self-interest is wrong and misses a critical ingredient for economic success. Markets grow in what Professor McCloskey calls "ethical soil." Many economists now accept that virtues support the market; she upends that notion to declare, "The market supports the virtues." In other words, capitalism not only thrives in an atmosphere of prudence, temperance, and justice, but also can foster those qualities and other moral virtues, including love.

The "bourgeois" alluded to in the book's title is the citizen or businessperson in a capitalist society. The seven virtues she identifies are drawn from the classical and the Christian traditions; they meld the philosophical, the religious, and the commercial.

In an era when executives are trying to figure out how to succeed as they face constraints on all sides — from regulations such as Sarbanes-Oxley, on the one hand, and a relentlessly competitive global market, on the other — Deirdre McCloskey points to a seemingly counterintuitive solution. She agrees with the contention, put forth by the corporate social responsibility movement, that doing right by the customer and the community is the surest path to doing well. She acknowledges that many companies embrace this approach during good times, and quickly abandon it as an unaffordable luxury during bad times.

But Professor McCloskey's reasoning, based on an analysis of economic history, is novel: Companies do well in the long run *only* by doing good. Nobility of character is a core requirement for business success. If executives were more conscious of that — if they operated with integrity, focused on the customer, and were more sensitive to the needs of all stakeholders — their companies could be more profitable and have greater impact. At their best, she says, businesspeople often promote virtues in ways they may not even realize. Their actions and transactions can actually model virtue; the right kind of acquisition can exemplify Professor McCloskey's ideals of prudence, justice, courage, and hope. As she writes in the foreword to *The Bourgeois Virtues,* "we sometimes become good by doing well."

### Equal-Opportunity Iconoclast

Deirdre McCloskey, age 63, has long embraced contradiction. She is both a prominent economist and a leading critic of her profession. She has traveled the political spectrum: first a Marxist student at Harvard, then a Keynesian, and, eventually, a libertarian who landed in the economics department at the University of Chicago. She produces work of epic sweep, even as she burrows deep into the arcana of her discipline. With *The Bourgeois Virtues* making its debut, she is seeking a publisher for *Size Matters,* a polemic against the widespread use of statistical significance testing in economic analysis. But perhaps the most dramatic example of Professor McCloskey's fearlessness is that she started life as a *he.* Having made a successful career as Donald McCloskey, the economist underwent sexual reassignment in the 1990s and emerged as a woman. Along the way, Deirdre has challenged many of the economic, philosophical, and religious axioms that Donald held dear — all without losing a step professionally.

Professor McCloskey is one of "the broadest-gauged intellectuals I know," says Robert Fogel, a Nobel laureate who was Professor McCloskey's mentor at the University of Chicago. "There are one or two in my generation that are her match," he adds. Indeed, her intellectual journey has taken her through rhetoric, philosophy, the classics, and literature. By bringing a multidisciplinary approach to the study of economics, Professor McCloskey is hoping to inspire a change in the profession at large so that it better reflects society and can be more useful in solving complex human problems. Professor Fogel notes, "Everything that Deirdre has touched is interesting. It's insightful. It's provocative. Even if I don't agree with it, I have to worry about it."

Professor McCloskey's reputation is built on disputing the status quo. In the 1960s and 1970s, Donald McCloskey helped pioneer the field of cliometrics, an approach applying quantitative analysis to the study of economic history. In the 1985 book *The Rhetoric of Economics*, he issued a challenge to the economic formalists, the "Samuelsonians" whose mathematical models and abstract theory dominated the discipline's mainstream. Persuasion, he said, is as influential as so-called scientific analysis in shaping economic discourse. Though it remains outside the prevailing current of economic thought, *Rhetoric* is now considered a classic text in the field. Stanley Fish, the eminent social and literary theorist who brought Professor McCloskey to the University of Illinois in 1999, calls her an "intellectually curious and capacious" thinker along the lines of Thomas Kuhn in science or Richard Rorty in philosophy; she has raised fundamental questions about the underlying protocols, assumptions, and hard-science credentials of economics.

Through the breadth and depth of Professor McCloskey's work and prodigious writings runs a commitment to pragmatism and empirical research. She insists on embracing the messy complexities of human behavior, rather than relying on what she sees as the simplistic theoretical lens of modern economics. In her broadest critiques, she rails against the caricature of "economic man" — a self-interested hunter-gatherer whose only motivation is accumulation — that has been the mainstay of capitalist economics since Hobbes and Bentham. "Surely there is an opportunity to get rid of that great stick of a character, *Homo economicus,* and to replace him with somebody real, like Madame Bovary," wrote Professor McCloskey in *The Rhetoric of Economics.*

In *The Rhetoric of Economics*, Professor McCloskey also suggested that modern economics is based on a fundamental misunderstanding of the role that "rationalism" plays in the intellectual roots of capitalism. This misunderstanding has led both capitalism's critics and its defenders to the reductive misunderstanding of capitalism as a purely utilitarian, amoral system that glorifies personal gain at the expense of societal cooperation. Such a view, Professor McCloskey says, is dangerously wrong because it prevents capitalism from achieving its potential to foster virtue and economic growth.

Today, as scandals play out across the business pages, the view of capitalism as an engine of virtue feels counterintuitive to many. Such writers as Jack Bogle, founder of the Vanguard group of funds, pollster Daniel Yankelovich, and ethicist Lynn Sharp Paine have recently taken up the subject of corporate behavior. The premise of most of their work is that the greed inherent in the market must be tamed by outside forces (either laws or norms). In contrast, Professor McCloskey notes in *The Bourgeois Virtues* that classical capitalism, as envisioned by Adam Smith, has the seeds of morality already embedded in it and that no economic system is inherently good or evil. "The Capitalist Man in his worst moment is greedy," writes Professor McCloskey. "And so are you and I. And so, I note, is Socialist Man, in more than his worst moments."

The question, she says, is not whether greed is natural — or even good — but whether it adequately explains capitalist behavior. After all, commerce is as old as human civilization. Yet only in the last few hundred years has commerce, as it has developed in capitalist democracies, created richer societies governed by the rule of law. Those societies are better than the alternatives, argues Professor McCloskey, noting that since 1800, as the amount of goods and services produced and

**The question is not whether greed is natural — or even good — but whether it adequately explains capitalist behavior.**



consumed worldwide has risen eightfold, capitalism has emancipated women and slaves and, in most respects, contributed to societal freedom.

In Professor McCloskey's view, capitalism has made most people in the West better off. Instead of laboring in miserable conditions, most Americans and Europeans enjoy their work. Capitalism, she writes, has fostered "the doctor's love for healing…the engineer's for building…the soldier's for the fatherland…the economic scientist's for the advance of economic science."

None of this is new, says Professor McCloskey. Adam Smith was the first to posit that love of fellow humans is, contrary to the thinking of modern economists, not equivalent to self-love. Professor McCloskey recalls a famous passage in Smith's *The Theory of Moral Sentiments,* in which he asks why a person might sacrifice a finger to save an entire race of people: "What is it…which prompts the generous upon all occasions, and the mean upon many to sacrifice their own interests to the greater interests of others? It is not…that feeble spark of benevolence…. It is reason, principle, conscience, the inhabitant of the breast…. The natural misrepresentations of self-love can be corrected only by the eye of this impartial spectator."

Professor McCloskey reminds her readers that Adam Smith was a professor of moral philosophy who believed, as she puts it, in a "balanced set of virtues" and based his assumptions about capitalism on that balanced set of beliefs. But the belief in an ethical framework of Aristotelian and Christian virtues was replaced, in the 19th century, by utilitarianism — the view that the good is what brings the greatest happiness to the greatest number of people. From utilitarianism came the emphasis on material values that underlies laissez-faire economics.

Professor McCloskey calls for a return to the more nuanced Smithian view of capitalism — one that incorporates the S-values (*s* for sacred and sympathy), which she says account for the less "rational" workings of commerce, such as conversation, negotiation, and trust. These S-values, in combination with the P-values of profit and prudence, help explain how capitalism works at its best. From these values spring the bourgeois virtues of trust, which enabled early financiers from the Medicis to the Rothschilds to flourish (the word *credit,* notes Professor McCloskey, is rooted in the Latin word for trust), and community-mindedness, which led ship owners to voluntarily pay fees for the support of private lighthouses in pre-19th-century Britain. Other historical examples of bourgeois virtue include tithing, which prompted most middle-class 19th-century Americans to give 10 percent of their incomes to charity. Similarly, in 17th-century Amsterdam, the public purse supported 10 percent of the population.

"Smith got it right and the later economists and calculators have got it wrong," writes Professor McCloskey. "You can't run on prudence and profit alone a family or a church or a community or even — and this is the surprising point — a capitalist economy."

Politically, Professor McCloskey regards herself as an ardent but atypical libertarian. She abhors government, not because she regards it as overbearing but because it has not done a good job of helping to alleviate the plight of the poor. She supports steep inheritance taxes, state-financed early childhood education, and a regular stipend for citizens (like that recently proposed by writer Charles Murray) instead of Social Security. She writes: "I would nonetheless have to note with Robert Nozick that the taxes to pay for…ideas, good or bad, are a kind of slavery. But I would be a more cheerful slave if my masters…were actually the poor."

According to Professor McCloskey, the better that government works, the more likely it is to be hijacked by special interests that serve the wealthy. There is a middle ground, she says, between communitarianism and unbridled individualism, one that recognizes "a positive duty to be a good bourgeois.… Placing duties ahead of rights comes naturally to a burgher of Delft or to a citizen of Rapid City," she writes in *The Bourgeois Virtues.*

**Finding Herself**

Professor McCloskey's intellectual journey began in the 1960s at Harvard, where Donald McCloskey, the son of a Harvard professor, was a left-leaning undergraduate and graduate student. His pioneering work with cliometrics to explain British economic history drew the attention of Robert Fogel of the University of Chicago and led to a faculty appointment there. In Chicago, Professor McCloskey became a proponent of a rational and utilitarian view of both man and markets, and his ideas flourished in an atmosphere of academic eclecticism and intensity. Professor McCloskey ate lunch regularly with the finance pioneers in the business school, including Fischer Black, Eugene Fama, and Merton Miller, whose ideas about risk and portfolio balance influenced the work that won Professor McCloskey tenure: He studied the geographically scattered holdings of British peasants prior to the enclosure movement of the 17th and 18th centuries — a seemingly irrational arrangement that forced farmers to walk long distances and exposed them to the "externalities" of the farmers who managed neighboring plots. (For example, if a farmer failed to weed his own plots, the weeds might encroach on the surrounding properties.) Yet Professor McCloskey discovered that scattered plots proved to be a sensible form of risk insurance; a diversified portfolio of lands could insulate individuals from disaster due to variable soil and weather conditions.

By the time Donald McCloskey had won tenure in the mid-1970s, he'd already started building his reputation as a gadfly. While agreeing with many of the substantive positions of his colleagues, Professor McCloskey came to view their methods as narrow and their certitude as suspect. "They'd base an argument on the premise that such-and-so industry is perfectly competitive," recalls Professor McCloskey. "And I got to be a pain in the neck in seminars by asking, 'How do you know that this industry is perfectly competitive? What's your evidence?' And they'd look at me cross-eyed."

By the late 1970s, Professor McCloskey had begun to have doubts about economics as it was practiced at the University of Chicago and other elite institutions. He had become suspicious, as his friend and fellow

## Deirdre McCloskey's Seven Bourgeois Virtues

1 **Prudence** not just to buy low and sell high, but "to trade rather than to invade, to calculate the consequences, to pursue the good with competence."

2 **Temperance** "to save and accumulate, of course. But it is also the temperance to educate oneself in business and in life, to listen to the customer humbly, to resist the temptations to cheat, to ask quietly whether there might be a compromise here."

3 **Justice** "to insist on private property honestly acquired. But it is also the courage to pay willingly for good work, to honor labor, to break down privilege, to value people for what they can do rather than for who they are, to view success without envy."

4 **Courage** "to venture on new ways of business. But it is also the courage to overcome the fear of change, to bear defeat unto bankruptcy, to be courteous to new ideas, to wake up next morning and face work with cheer."

5 **Love** "to care for employees and partners and colleagues and customers and fellow citizens, to wish well of humankind, finding human and transcendent connection in the marketplace."

6 **Faith** "to honor one's community of business. But it is also the faith to build monuments to the glorious past, to sustain traditions of commerce, of learning, of religion."

7 **Hope** "to imagine a better machine. But it is also the hope to see the future as something other than stagnation or eternal recurrence, to infuse the day's work with purpose, seeing one's labor as a glorious calling."

Source: Deirdre N. McCloskey, *The Bourgeois Virtues: Ethics for an Age of Commerce* (University of Chicago Press, 2006)

Deirdre McCloskey finished her work on *The Bourgeois Virtues* while teaching at Erasmus University in Holland



economist Arjo Klamer puts it, of its "aura of science" and illusion of exactness. His repeated call for economists to be more empirical, "to stop talking endlessly about the realism of assumptions and go out and measure," as Professor McCloskey puts it, led to run-ins with colleagues, especially Robert Lucas and George Stigler, Nobel laureates who dominated the department. With the departures of his mentor, Robert Fogel, and with those of Milton Friedman and Gary Becker, the gadfly's disillusionment only grew.

In the midst of this turmoil, Professor McCloskey developed a friendship with Wayne Booth, one of the 20th century's most prominent literary critics. Professor Booth, also on the faculty at Chicago, asked Professor McCloskey to give a lecture to his undergraduates on the rhetoric of economics; Professor McCloskey agreed and then realized he had to figure out what that was. The discussions with Professor Booth eventually developed into *The Rhetoric of Economics,* in which Professor McCloskey deconstructed the writings of leading economists and argued that the mathematical methods of the profession are actually metaphors that serve as both a tool of persuasion and a powerful barrier to entry against speakers of plain English. Professor McCloskey further argued that the metaphors are not neutral, as has long been assumed; some, such as the "invisible hand," Adam Smith's mechanism by which an individual acting in his or her own interest is also helping the community, are subtly ideological. Others, such as the more startling metaphors of Gary Becker, who has likened children to

**There is a middle ground in capitalism in which "placing duties ahead of rights comes naturally."**

durable goods because, like houses, they are "expensive to produce and maintain" and, like refrigerators, "they have a poor secondhand market," are explicitly utilitarian. In Professor McCloskey's world, the power of economists rests on the rhetoric. It's not that their arguments are necessarily right analytically; it's that they're persuasive.

By the time Professor McCloskey published his book on rhetoric, he had left the University of Chicago. A promotion to full professor had been slow in coming. So in 1980, when J. Richard Zecher, a friend and colleague who had left the University of Chicago years earlier, became dean of the business school at the University of Iowa and offered Professor McCloskey a full tenured professorship in both economics and history, he jumped at the chance.

While some economists dismissed Professor McCloskey's book on rhetoric as a frivolous digression, others hailed it as an important step forward in the field. "Her economic rhetoric work is interesting and of considerable value," says Gary Becker. "She's right that opinions are influenced not just by scientific example, but also by rhetoric."

*Rhetoric* put Professor McCloskey on the front lines of a mounting attack against the formalism of modern economics. Another influential book that was published shortly after *Rhetoric, The Making of an Economist,* by Arjo Klamer and David Colander, was based on a study of graduate students in economics and concluded that although only a tiny minority — 3 percent — of the students surveyed considered a "thorough knowledge of the economy" important to success in graduate school, well over half considered excellence in mathematics to be very important. The study underscored Professor McCloskey's argument that economics had drifted too far from empirical research on real-world problems. The Klamer–Colander study also led to the appointment of a commission on graduate education in economics by the American Economic Association, which issued a report in 1991 that concluded, in part, that graduate programs generate "too many *idiots savants,* skilled in technique but innocent of real economic issues."

As the debate about *Rhetoric* and the direction of the economics profession raged in academic circles in the early 1990s, Professor McCloskey was on the cusp of another radical change — this one far more personal. Professor McCloskey was married with two grown children and teaching at the University of Iowa when he began cross-dressing regularly, surfing Internet sites for cross-dressers, and visiting transvestite bars in Chicago. Professor McCloskey, who in the book *Crossing: A Memoir* describes a compulsion to cross-dress from an early age, began the process leading to a sex change.

Few who knew Professor McCloskey anticipated the change. Friends noted that the McCloskeys seemed to be an unusually close couple. Today Professor McCloskey says that she was never explicitly unhappy. But there were signs of anxiety. Claudia Goldin, a former student of Professor McCloskey's and a labor economist at Harvard, recalls that, at the University of Chicago, Donald McCloskey had been a "a psychological train wreck. He was trying to be too much of a man, yelling and screaming all the time."

Today Professor McCloskey is a gracious, even-tempered woman — by many accounts, more amiable than Donald was. "My wife disliked Donald, but she loves Deirdre," says Arjo Klamer, who holds a chair in the economics of art and culture department at Erasmus University in Rotterdam. Professor McCloskey readily

# In Defense of "Noisy Data": Deirdre McCloskey's Campaign against Significance Testing

Deirdre McCloskey's faith in pragmatism and empirical research also fuels *Size Matters,* her unpublished work that attacks a small but essential rivet that holds together much of accepted modern economic research — significance testing. The idea comes from the field of statistics and holds, roughly, that an effect is significant if there is less than a 5 percent likelihood that it occurred by chance. The book, which Professor McCloskey coauthored with her former student Stephen T. Ziliak, now a professor at Roosevelt University in Chicago, explores how economists have come to mistake statistical significance for economic significance, and how that confusion has led to vast amounts of economic research that is irrelevant or can lead to poor economic policy. They argue that instead of relying on the on–off switch of statistical significance, economists should calculate the costs of being wrong, and use those criteria to help set significance levels. Statistical significance testing, say Professors McCloskey and Ziliak, is too mechanical to be used as a decision-making tool; the considered judgment of scientists, which is messier and less formulaic, would ultimately yield better results.

For example, in the early 1980s, the state of Illinois developed a marginal-wage subsidy program designed to reduce the time that workers would need to collect unemployment insurance. The researchers who tested the pilot program determined that the average benefit-to-cost ratio was 4.3 to 1, meaning that Illinois reduced its spending on unemployment insurance by $4.30 for every $1 spent on the subsidy. However, the researchers determined that the finding was not *statistically* significant because there was too much "noise" around the data: Instead of the 5 percent significance level, the data showed a 12 percent possibility that the reduction in unemployment insurance might have been caused by something other than the marginal-wage subsidy.

"These nitwits said: 'No. Not worth it! It's insignificant.' It's a perfectly clear example of this confusion between fit and substance," says Professor McCloskey. "If you're the governor of the state, you're a sophisticated person, you don't ask for guarantees. What you want to know is whether it's worth doing this program." It obviously is, says Professor McCloskey, who adds that any reasonable interpretation of the data would conclude that the possibility of a four-to-one benefit-to-cost ratio was too valuable to discard because of a 12 percent risk of being wrong. The correct course of action, contend Professors McCloskey and Ziliak, would have been to continue the wage subsidy while conducting empirical research to determine the other factors that might have influenced a drop in unemployment spending.

The misuse of significance testing extends into other realms, like medicine, with sometimes devastating costs. Epidemiologists blame the test for the abandonment of such treatments as flutamide, which has shown promise for patients with advanced prostate cancer. A controversial National Institutes of Health study on women's health concluded that eating a low-fat diet does *not* reduce cancer risk even though subjects who avoided fat clearly showed a 9 percent lower risk of contracting breast cancer; critics of the study point out that the finding was dismissed because the results just missed the threshold of statistical significance — not because the low-fat diet was ineffective. "If more women had been studied or the study had gone on just a little longer, the data very likely would have been statistically meaningful and announced as such," one biostatistician said in a February 2006 article in the *Wall Street Journal*.

**— A.G.**

admits that while Donald wouldn't hesitate to "slip a knife" into an opponent, Deirdre would never do that. "I'm nice to everyone, whereas Donald wasn't," says Professor McCloskey. "The personality I now have is very much what I had before adolescence."

The Klamers helped Professor McCloskey make the transition to womanhood. Professor Klamer arranged for Professor McCloskey to get the first of what would be several visiting professorships at Erasmus University in Holland, where, she says, she could make her transition in an atmosphere of tolerance. Professor McCloskey's family was not so supportive. Deirdre's sister, a Harvard psychologist, tried to have her institutionalized twice — once having her hauled off from the Palmer House in Chicago where she was attending the annual meeting of the Social Science History Association. Professor McCloskey's former wife, with whom she wished to maintain a friendship, has cut her off entirely, as have her children. While Professor McCloskey has rebuilt ties to her sister and other relatives, her mother was the only member of the immediate family who remained loyal throughout the change.

After Holland, Professor McCloskey returned to Iowa for another three years, in part to prove that she could be accepted as a woman in an institution that had gotten to know her as a man. But in 1999, Professor McCloskey was ready for a change when Stanley Fish recruited her to the University of Illinois in Chicago.

By most accounts, the gender change has not damaged Professor McCloskey's professional reputation. "Deirdre hasn't suffered at all," says Stephen T. Ziliak, her collaborator in the critiques on significance testing. "Economists, in particular, are very libertarian. Even if not in their scholarship, they are in their personae." Professor McCloskey herself notes wryly that when she told Gary Fethke, the dean of the University of Iowa business school, about her impending sex change, Dean Fethke responded: "Thank God…I thought for a moment you were going to confess to converting to socialism."

In many ways, Professor McCloskey's transformation from man to woman mirrors the dramatic transformations in her thinking that gelled as Donald became Deirdre: from Marxist into capitalist libertarian, from atheist into practicing Episcopalian, and from cliometrician, using mathematical models to understand economic history, into critic of significance testing in economics. Although Deirdre McCloskey's work is a logical outgrowth of Donald McCloskey's, it is also in some ways a rejection of it.

Professor McCloskey's intellectual odyssey is not yet over. It took her six years to recognize that if economics is rhetorical, then it cannot be wholly rational. She acknowledges that she took a long time to move away intellectually and emotionally from her views as a "positivist, straight-line scientist" and assumes that her intellectual journey will cover still more ground. She has only just begun to define an economics that balances mathematics-based theory with a more qualitative approach.

As Professor McCloskey continues to work on the future volumes of *The Bourgeois Virtues,* she remains optimistic about capitalism and her profession. "This long episode of [the] machine, of faith in mechanical views of what humans are like, may come to an end eventually," she says. "I dream of an economics that will not throw away the insights that have been provided by people like Samuelson…but will redo them for human beings." In achieving that dream, she can lead academic economists to a new perspective that will allow them to develop a more complete view — and greater appreciation — of human endeavor in a business setting. +

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## Resources

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Ann Graham, "Lynn Sharpe Paine: The Thought Leader Interview," *s+b,* Summer 2003, www.strategy-business.com/press/articles/22047: Research on ethical ambiguity anticipates some of Professor McCloskey's ideas.

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Deirdre N. McCloskey, *If You're So Smart: The Narrative of Economic Expertise* (University of Chicago Press, 1990): Argues that the power of economists rests more on their abilities to persuade than their abilities to predict the future.

Deirdre N. McCloskey, *The Rhetoric of Economics* (1985; University of Wisconsin Press, 2nd ed., 1998): How economic formalists have taken their reliance on econometrics and mathematical models "absurdly too far."

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Adam Smith, *The Theory of Moral Sentiments* (1759; Prometheus Books, 2000): Deirdre McCloskey credits the father of modern economics with much of her thinking on the virtues of capitalism.

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