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SHORT REVIEWS

IOANNIS THEODOSSIOU, *Wage Inflation and the Two-Tier Labour Market*, Aldershot, Hants; Avebury, December 1992, pp. xviii + 253, £35.00 (hardback).

This book stems from a dissatisfaction with neoclassical and Keynesian descriptions of the labour market at both micro and macro levels. Unhappy with natural rates of unemployment, unexplained wage floors and the emphasis on real wages, Theodossiou has produced an institutional analysis which runs freely from firm-worker relationships to a theory of wage inflation.

The book's approach is behavioural and purely descriptive for the bulk of the analysis. The initial assumption is of imperfect and asymmetric information. This means that long-term relationships with potential benefits for employer and employee hold contractual risks for both. Imperfect data on employers make workers wary about accepting wage offers from firms with no reputation for 'fair' treatment. Heterogeneity of workers means the true ability of employees may only be revealed slowly.

Theodossiou argues that this uncertainty leads both parties to indulge in heuristic searches for partners; moreover, initially fragile relationships improve over time as the mutual benefits and costs of separation increase. A discussion of searching develops naturally into a description of career labour markets governed by implicit contracts. However, Theodossiou notes that, for some jobs, contractual benefits are small compared to the flexibility of neoclassical auctions. In this second tier, employment strategies are more short-term and reflect the prevailing market conditions. The career and non-career markets are identified roughly with non-manual and manual occupations.

The differing behaviour of these two tiers has asymmetric macroeconomic effects. 'Fair' treatment in the career market leads to inflationary 'norms' in wage bargains which only evolve slowly. This inherent inertia makes wages inflexible, but Theodossiou argues that this is only one-way. A sustained expansion in demand leads initially to increased recruitment in the career sector and ultimately to wage rises in both sectors, as relative wages are the key element. However, falling demand leads to dismissal and layoffs in the non-career market initially. A prolonged recession may lead to 'last in, first out' redundancies in the career sector but is unlikely to manifest itself in a fall in career wages. Therefore sustained wage inflation is attributable largely to the career sector; unemployment falls first and most heavily on the non-career sector.

Theodossiou formalises this theory econometrically and estimates determinants of wage inflation. However, the results, although supportive, are unconvincing. The estimator is crude, and the data unappealing. Causation, cointegration and simultaneity in wages, prices and employment is theorised away, and specification tests are very basic.

The effect is to mar an otherwise interesting book which is well developed, fairly comprehensive in the treatment of searching and implicit contracts, and readable. It continually emphasises observed behaviour: the importance of nominal and relative wages, uncertainty, reputation, and the establishment of customary practices. As an alternative to mainstream labour market theory (and an adjunct to search theory) the book has considerable merit, and the unprepossessing econometric evidence should not detract from this.

Two minor warnings: the book has a large number of typos—including, at one confusing point, the substitution of employer for employee; and authors are often indexed incorrectly.

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S. A. DRAKOPOULOS, *Values and Economic Theory: The case of hedonism*, Avebury, 1991, pp ix–235, ISBN 1 85628 200 7.

Can Economics, as a 'scientific' discipline, lay claims to be 'value free', either now or in the past? In particular (and in order to ask a question that is better capable of constructive discussion), how far is it true that 'orthodox' economics assumes economic behaviour to be egoistically and hedonistically motivated? In his book, Drakopoulos leaves us in little doubt that egoistical hedonism was and still is of considerable significance in economic theory. Now, this of itself does not, I submit, establish that economic analysis is value ridden, unless practising economists deny these elements in their theories, and in fact economic behaviour is grounded in such behavioural imperatives. Thus, if economic behaviour is e.h.m. (egoistically and hedonistically motivated), and analysts deny such, then presumably they are either mad or find e.h.m. so distressing that they can't bear to recognise it, which latter appears to me to be a whopping value judgement. The truth of the matter, argues Drakopoulos, is that economists convince themselves that their models are value free in the sense that logical positivism (or some such) is all that is needed for economic analysis. And then, argues Drakopoulos, the very same economists construct models that, at bottom, depend upon e.h.m. Do they know what they do, or can only Lewis Caroll explain this strange group of eggheads?

There is a very serious political point here. I tell my students that if an economist is asked to advise on economic policy he will do so on the basis of models that embody maximising principles, and these models assume e.h.m. The alternatives put forward, be the economist ever so 'neutral', are compared in terms of e.h.m. aggregates of one kind or another. And, yet, as Drakopoulos affirms, there are many alternative ways in which economic behaviour could be analysed, (and perhaps more realistically and with greater powers of prediction). There would then be different biases when it comes to policy evaluation. So in this sense, perhaps it is laudable that economists have, for the past hundred years, tried to divest themselves of e.h.m.

In order to examine whether economics analysis is based on e.h.m. one requires both a good knowledge of the current state of the orthodoxy and a good knowledge of how it arose. (One cannot even begin to understand the present without knowledge of the past). Thus, Drakopoulos's book devotes much space to the history of economic and utilitarian thought. He ranges, highly successfully, from Plato to Arrow. The exposition of different types of hedonism, from the ancient Greeks, the Cyrenaics, the Epicureans, through Hobbes, Helvetius, Bentham and on to Edgeworth and Hicks, though it has been done before, is very well and illuminatingly done here.

The author is equally sure footed when he examines the underlying assumptions of theories that claim to divest themselves of the unwanted value assumptions. Thus, the rationality postulate in consumer theory is shown to rely on Archimedian preferences, such that all choices are reducible to a common denominator, which together with choice consistency and the maximisation assumption, strongly points to the abiding influence of e.h.m. as the behaviourist assumption. The tangles into which Hicks and Samuelson put themselves are also convincingly portrayed. (It is interesting that the 'behaviourist' Samuelson reacted so adversely to Friedman's 'instrumentalism', unattractive though the latter is).

One of the many fundamental questions touched on in the book is whether 'value free' economics is possible, especially in view of the serious doubts expressed recently as to whether even the physical sciences can be value free. On a very mundane level, suppose economists became entirely positivist, i.e. based theories only on observations. If it is possible (which is doubtful) to make value free observations, surely all one could then do is to draw correspondences, with no explanation of events. Of course, econometricians uses the term 'explanation' in this correspondence sense but even they often assume some maximising behaviour in their starting off equations. More interestingly, Drakopoulos points to alternative theories of choice behaviour (which appear to be more empirically sound than those based on the maximization hypothesis) as being suitable candidates for new approaches in economic theory. It may also be mentioned here that not only are the obvious candidates such as Marx, the Historicists and Veblen pointed to as offering alternative approaches to e.h.m. in the study of economic phenomena, but within the pantheon of 'orthodoxy', Adam Smith, Marshall and Keynes all feature.

The book is well and clearly written (apart from at the very beginning) and it is a considerable achievement to cover ground that can be slippery and complex in so lucid a manner. Drakopoulos has written a wide ranging book, and one that is useful as a reference source as well as telling its particular stories. It is certainly a book that can be read with advantage by economics undergraduates, to compensate for the inevitable narrowness of mainstream economics courses. It would also be of interest to other social scientists and I would also hope that main stream academic economists would find time to read it. All in all the book is to be welcomed and Drakopoulos congratulated.

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