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Accounting at the Heart of the Performativity of Economics

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Recent research has demonstrated the performative power of economics, in the sense that economic theory tends to mould the world to itself and its descriptions. The role of accounting in the performativity of economics is highlighted below.

The idea of the performativity of economics

The concept of performativity comes from linguistics, most significantly the work of J.L. Austin, and was introduced into economic sociology by Callon (1998) and MacKenzie (2004). D. MacKenzie (2004: 305) proposes two meanings for this notion. The first, *generic performativity*, points to the fact that the categories of social life “*are not self-standing, natural or to be taken as given, but are the result of endless performances by human beings and (an actor-theorist such as Callon would add) by non-human entities and artefacts as well. (...) In this meaning, performativity is at the most general level entirely obvious. (...) Except in areas such as sex and gender where social categories might be read as natural, generic performativity is a weak claim (could matters be otherwise?) but still empirically important.*” The second meaning of performativity, *Austinian performativity*, is less universal but stronger. In this sense, “*a performative utterance is one that makes itself true, that brings into being that of which it speaks, as when a monarch designates someone an outlaw, an appropriate authority designates a couple husband and wife.*” MacKenzie then uses this definition to study the performativity of models in financial economics (p. 306). “*To ask whether a model in financial economics is performative in the Austinian sense is to ask, among other things, whether the effect of the practical use of the model is to change patterns of prices towards greater compliances with the model.*” More recently, Mackenzie, Muniesa and Siu (2007) have dedicated a whole book to the question of the performativity of economics.

Exploring this research agenda, I rely in this contribution on the Austinian meaning and argue that accounting helps to make economics performative, being one of the instruments through which economics can make the world conform more closely to its descriptions.

Two phenomena are important to understand this role of accounting. The first is the longstanding relationship between accounting and economics: the former has supplied many concepts for the latter, such that the latter’s performative power partly depends on its capacity to latch on to *native* representations in the world, constructed by businessmen and tradesmen. Partly fluent in accounting language, economics has *adopted* accounting practices to bring its revised economic concepts into being. A second dynamic lies also in the relationship between accounting and economics, notably whenever economics parts company with or opposes accounting concepts. In a reversal of influence, economic concepts are introduced into accounting frameworks via a new discipline originating from the early 20th century, accounting theory, which has translated economic concepts, originally foreign to accounting, into accounting concepts. Both phenomena are studied below.

Accounting as an inspirer of economics

The fact that accounting practices were a major source of inspiration for the earliest economists (especially classical economists) hardly needs further demonstration (Klamer and McCloskey 1992; Thompson 1998). Accountants and economists share the same vocabulary: costs, expenses, investments, capital, assets, revenues, balance sheet, budget, expenditure, profit, etc.

The concept of capital that is central to economics is also central to, and in fact comes from, accounting. Italy supplied the first occurrence of the word *capital* in an economic sense in a Florentine accounting ledger dating from 1211. The term then appears to have spread within commerce and banking from Italy throughout Europe (Braudel 1981). In order of historical appearance, the economic meanings¹ of the word *capital* have been:

- The amount of money loaned as opposed to the interest on the loan.
- The money invested in a trading concern or funds contributed by a merchant to his new concern. This second meaning is the closest to the accounting meaning.²
- By extension, for late 18th century economists, capital meant all wealth invested in the economy for production. Here, the term became dissociated from the idea of an amount of money, covering all sorts of wealth and capital goods. This extension caused a frequent confusion between the meaning of capital in the sense of *money invested*, and in the sense of *the things* in which money is invested, since economists did not always explain their positions despite the significant consequences (Hicks 1974). This confusion never arose for accountants trained in double-entry bookkeeping, for the accounting model makes a clear distinction between the two meanings, which are also represented by the two sides of the balance sheet.³

Further, regarding the influence of the accounting framework on the birth of economic thought, I have shown elsewhere (Chiapello 2007) that Karl Marx took a close interest in accounting, helped by his friend Friedrich Engels who was aware of the cutting-edge practices of Manchester manufacturers. Marx sought to define the specific characteristics of capitalism and needed to recreate an interrelated system and its dynamics. For this systemic understanding, the representation of circulation and accumulation in accounting terms played a central role. For a mid-19th century observer such as Marx, the language of accounting was similar to that of political economy, a field in which he read every work published. Capital, profits, and wages were concepts common to accounting and the political economy of his time. Marx would choose the closest economic concepts possible to accounting.

The importance of accounting in the genesis of economic concepts is thus clearly visible in the works of the *classical economists*. They borrowed accounting terms and concepts very consciously. Yet, once introduced into economic thought, these concepts began to lead an autonomous life, progressively diverging from their roots.

In contrast with classical economics, neo-classical economics departs from traditional accounting representations of the economy. Irving Fisher's complete redefinition of the concepts of capital and income enabled, at least intermit-

tently, a divorce between accounting and economics (see e.g. Fisher 1906). Post-Fisher, capital is no longer backward-looking and seen as the money invested in capital goods or as the capital goods themselves, as conceptualized in accounting. It is now forward-looking and conceptualized as all future services expected of the capital goods. Discounted cash-flow calculation⁴ was then invented to operationalize the new economic concept of capital, and accounting, hitherto dedicated mainly to registration of past events, became a practice removed from neoclassical economic thinking.

But accounting frameworks played an important role at another moment in the history of economic thought: the construction of national accounts to provide statistical resources for Keynesian policies. As Vanoli (2002) and Studenski (1958) have explained, pre-1930s economic statistics used incomplete information or only attempted to estimate national income. It took time before the metaphor of business accounting was consciously used in constructing the model of national accounts (Suzuki 2003)⁵ and in systematic organization of statistical information in a coherent framework. This international effort was completed in the 1960s. Yet, since the 1980s, Keynesian macroeconomics has been in crisis, and accounting began to lose its attraction for many economists.

The moments of proximity, when economics refers consciously to business accounting to construct its own representation of the economic world, may explain the recurring temptation for economics to return some theoretical input into accounting, seeking to bring accounting into line or rationalize it in conformity with its own representations. Thus while accounting practices are not born out of economics – having on the contrary supplied some of its weapons – they may be influenced by economic theory. When accountants sought to rationalize practices and define their guiding principles, they turned to economics for the theoretical discourse that accounting should serve by operationalizing its concepts.

Accounting inspired by economics

Hopwood (1992) clearly identifies this movement. He stresses the grip of economic categories on accounting practice, and the demand placed on accounting to operationalize economic practices and reform in order to produce calculations that conform more closely to economics.

One of the most striking examples of the influence of economics on accounting concepts is the recent authorization in *International Accounting Standards* (IAS) of discounting future cash flows (DCF) as a valuation method for certain assets, in the pursuit of *fair value accounting*. This accounting policy assumes that the definitions of *Capital and Income* provided in the work of Irving Fisher are accepted by all. A few decades after economics, accounting is apparently undergoing its own revolution.

The story of this conquest by economic concepts is quite long. It begins with the birth of accounting theory in the 1920s, followed very closely by the creation of the first accounting standards in the US under the auspices of the new *Securities and Exchange Commission* (SEC). Accounting theorists, such as Littleton and Paton, wanted to give accounting theoretical foundations and influence accounting standard production as part of the mission of their newly created profession. Accounting theorists sought those foundations in economics, and organized many debates on Fisher's concepts and their possible translation to accounting. The tradition of dialogue between accounting theory and economic concepts then lasted up the 1970s (special mention must be made of R.J. Chambers, who can be seen as one of the fathers of fair value accounting).

The *positivist* revolution in accounting academia, inaugurated by Watts and Zimmermann's (1979) attack on the old school, changed everything. The positivists saw no point in thinking about what accounting should be, as accounting theorists did. Instead, in their opinion, a careful study of companies' actual accounting practices was needed. This new, highly aggressive generation of academics successfully discredited their predecessors and, to a large extent, put an end to accounting theory research. But the accounting standard-setting system was still developing and eager to take the old theories on board and re-establish its legitimacy after a series of scandals through the application of economic accounting theory. The newly created (1973) *US Financial Accounting Standards Board* launched its accounting framework project (Gore 1992; Zeff 1999) in the first manifestation of this trend, followed closely by other countries. The old accounting theorists' dream of influencing standard-setting became reality, strangely at a time when they were no longer welcome in academia. The unexpected destiny of accounting theory's efforts to bring accounting closer to neoclassical economics was also boosted by the rising influence of the financial

markets themselves and their penetration by Fisher's economic concepts.

The close historical relationships between accounting and economics, largely hidden because contemporary economists often know little about accounting, explain why accounting remains a good practical vector for pure economic concepts, such as the Fisherian concept of capital. This can be seen as a good example of accounting's ability to make economics perform the economic world.

Eve Chiapello is Professor at the HEC School of Management in Paris. Her research interests include accounting and the history of economic ideas, the sociology of accounting, and the historical transformation of management and capitalism. *Inter alia*, her articles have been published in the journals *Accounting, Organizations and Society*, *Critical Perspectives on Accounting*, *Berliner Journal für Soziologie*, and *Sociologie du Travail*. With Luc Boltanski she co-authored *The New Spirit of Capitalism* (Verso, 2006).

Endotes

1The economic meanings of the word *capital* should be distinguished from older uses, when as an adjective it was applied to crimes and punishments, or carried the most obvious meaning of *most important* (e.g. the capital city of a country).

2We talk here of the accounting concept of *share capital*, which represents the historical value of the contributions to the firm shareholders have made in the beginning and during the life of the firm by making external resources available to the firm. Shareholders' equity consists of two components, *share capital* plus *retained earnings* (or reserves). Reserves represent the accumulation of capital, the part of the value created through the firm's operations that shareholders have chosen not to take out of the firm.

3Assets, to be found on one side of the balance sheet, represent the value of the *things* in which money is invested. The money invested is represented on the other side of the balance sheet consisting of *shareholder's equity* plus *liabilities*, as the money invested comes from shareholders or other money bringers.

4The *discounted cash flow* (or DCF) approach describes a method of valuing a project (company or asset) based on 1) a forecast of all future cash inflows and outflows generated by the project at different periods of time, and 2) a transformation of these flows by the use of a discount rate supposed to give their value as if they occurred at a single point in time so that they can be compared in an appropriate way. The discount rate used is supposed to represent the cost of capital, and may incorporate judgments

of the uncertainty (riskiness) of the future cash flows. The evaluation of the value of an asset according to this method is thus based very largely on expectations about the future, neither on the money cashed out in the past to buy or produce it (as in the historical cost method) nor on the actual market value.

Suzuki (2003) shows how the history of British national accounting was of central importance to the development of macroeconomics, and reconstructs the early processes through which the notion and practice of modern macroeconomic management emerged.

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