

TSE DEEQA – Semester 2

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Paul Seabright

Advanced Behavioral and Experimental Economics

Weeks 1 & 2



The place of economics in relation to other social sciences

- The term “economics” appears to be derived from the Middle French “économiste”, meaning someone who manages a household budget frugally.
 - It’s hard to know when it first came to characterize a profession. The term “classical economics” was first used by Karl Marx to characterize Smith, Ricardo, Mill and Malthus. Burke’s famous lament in 1793 the “The Age of Chivalry is gone. That of sophisters, economists and calculators has succeeded; and the glory of Europe is extinguished for ever”, probably uses the older, now archaic meaning of the term.
 - However, a dominant narrative holds that Adam Smith was the first economist in the modern sense. What is meant by this?
-

An influential narrative: Heilbroner's *Worldly Philosophers*

- Published in 1953, the book has had seven editions (the last in 1999) and sold nearly 4 million copies, making it the second highest selling economics book of all time (after Samuelson's *Economics*).
- Told a “great men” history of economic thought starting with Smith.
- Argued that, even though “markets have existed as far back as history goes” the economy as such could not be a subject of study before Adam Smith, because
 - “The profit motive as we know it is only as old as modern man” (p.24).
 - “The Middle Ages, the Renaissance, the Reformation..could not envisage the market system for the thoroughly sound reason that that Land, Labor and Capital...did not yet exist....Land, labor and capital as agents of production are as much modern conceptions as the calculus” (p.27).

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Heilbroner's argument in more detail (I)

- “In primitive society, the struggle between self-centeredness and cooperation is taken care of by the environment” (p.19).
- “Under less stringent conditions, anthropologists tell us, men and women perform their regular tasks under the powerful guidance of universally accepted norms of kinship and reciprocity” (p.19).
- “Over the centuries man has found only three ways of guarding against (social breakdown)...he has ensured his continuity by organizing his society around tradition...or society can use the whip of authoritarian rule..the third solution to the problem of survival ...was called the ‘market system’” (pp. 19-20)
- “It was this paradoxical, subtle and difficult solution to the problem of survival that called forth the economists..but until the idea of the market system itself had gained acceptance, there was no puzzle to explain” (p.21).

Heilbroner's argument in more detail (II)

- Uses the preaching of Robert Keayne in Boston in 1639 that “to seek riches for riches’ sake is to fall into the sin of avarice”, to argue that “the idea of gain is by no means as universal as we sometimes suppose...the social sanction of gain is an even more modern and restricted development”.
- “While the idea of exchange must be very nearly as old as man...We must not make the mistake of assuming that all the world has the bargaining propensities of the modern-day American schoolboy...it is reported that among the New Zealand Maoris you cannot ask how much food a bonito hook is worth, for such a trade is never made and the question would be regarded as ridiculous” (p.27).
- “Lacking land, labor and capital, the Middle Ages, lacked the market(despite its colorful local marts and traveling fairs), society ran by local command and tradition... had Adam Smith lived in the years before 1400 he could have felt no need to construct a theory of political economy....there would be nothing for any economist to do for several centuries – until this great self-reproducing, self-sufficient world erupted into the bustling, scurrying, free-for-all of the eighteenth century” (p.29).

Heilbroner's argument in more detail (IV)

- Heilbroner mentions that Adam Smith was the author of *The Theory of Moral Sentiments* (1859) but does not discuss that book or otherwise consider its place in Smith's thought.
- Heilbroner's Smith is the Smith of the invisible hand, alive to the deficiencies of capitalism (monopolies etc) but most of all impressed by its incredible dynamism.
- Heilbroner's approach was for a long time followed by other historians of economic thought for whom the Smith of the *Theory of Moral Sentiments* was at most an irrelevance, perhaps even an embarrassment.
- We can now see a much greater continuity between the two works and a much greater continuity between Smith's writings and that of earlier scholars.

The two Adam Smiths?

- A tension between the author of *The Theory of Moral Sentiments* and that of *The Wealth of Nations*?
- Adam Smith and the tradition of “universal history”
 - What Smith inherited from that tradition.
 - What was new in Smith’s vision.
- The complex nature of sympathy, and its ambivalent coexistence with self interest.

Adam Smith on the tempering of selfishness by sympathy, from the very first sentence!

How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it – *The Theory of Moral Sentiments*, Part I, Chapter I



Adam Smith on the impartial spectator

Though it may be true, therefore, that every individual, in his own breast, naturally prefers himself to all mankind, yet he dares not look mankind in the face, and avow that he acts according to this principle.....When he views himself in the light in which he is conscious that others will view him, he sees that to them he is but one of the multitude....If he would act so as that the impartial spectator may enter into the principles of his conduct...he must... humble the arrogance of his self-love, and bring it down to something which other men can go along **with.** – *The Theory of Moral Sentiments*, Part II, Chapter II



How can we reconcile this with:

It is not from the benevolence of the butcher, the brewer, or the baker, that we can expect our dinner, but from their regard to their own interest.....

– *The Wealth of Nations*, Book I, Chapter II

A two-part answer

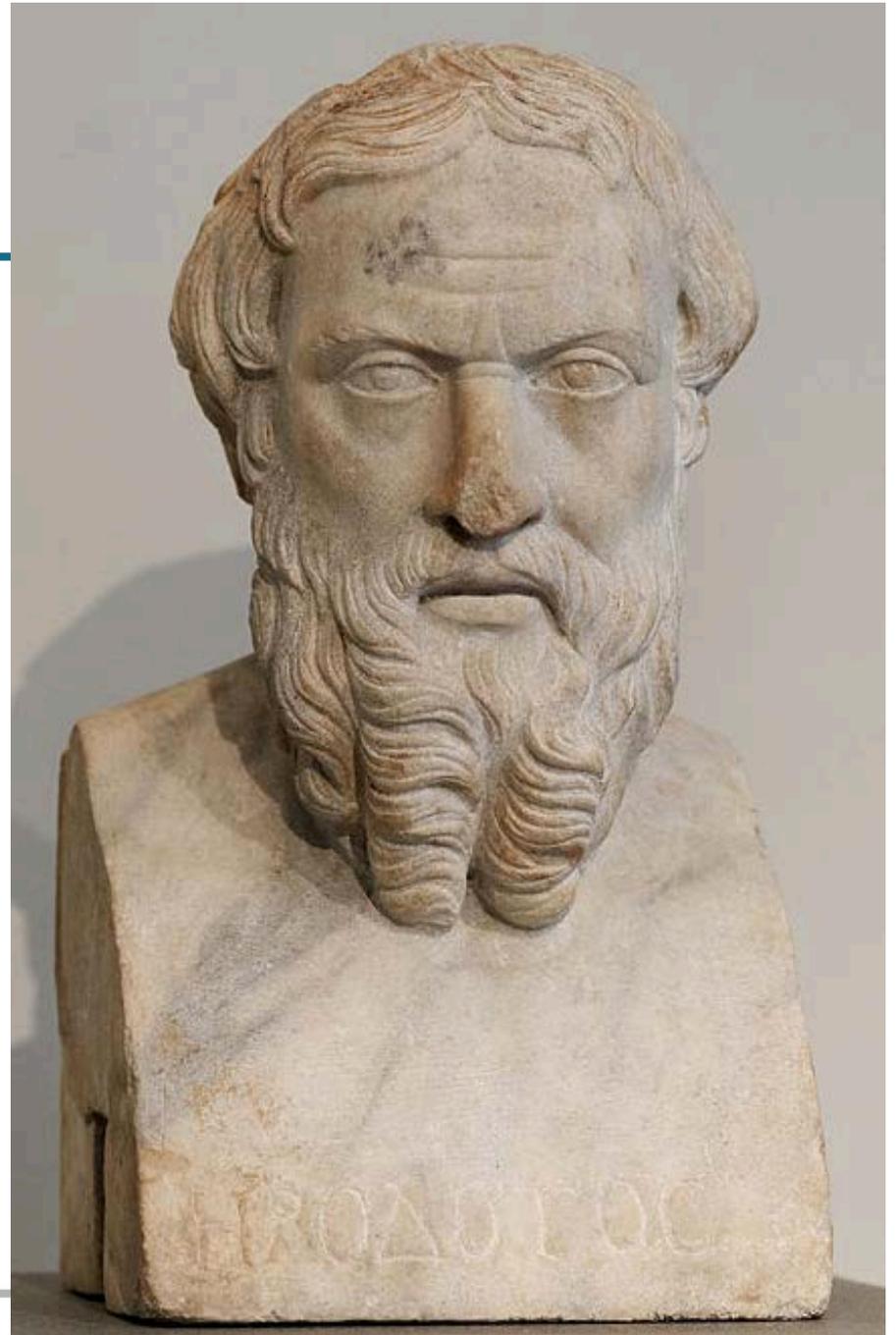
- Adam Smith and the tradition of “universal history”
 - What Smith inherited from that tradition: tension between the partial and the global perspective on society.
 - What was new in Smith’s vision: a radical insistence on the underlying unity of humankind, stronger than the differences between different peoples.
- The complex nature of sympathy, and its ambivalent coexistence with self interest.

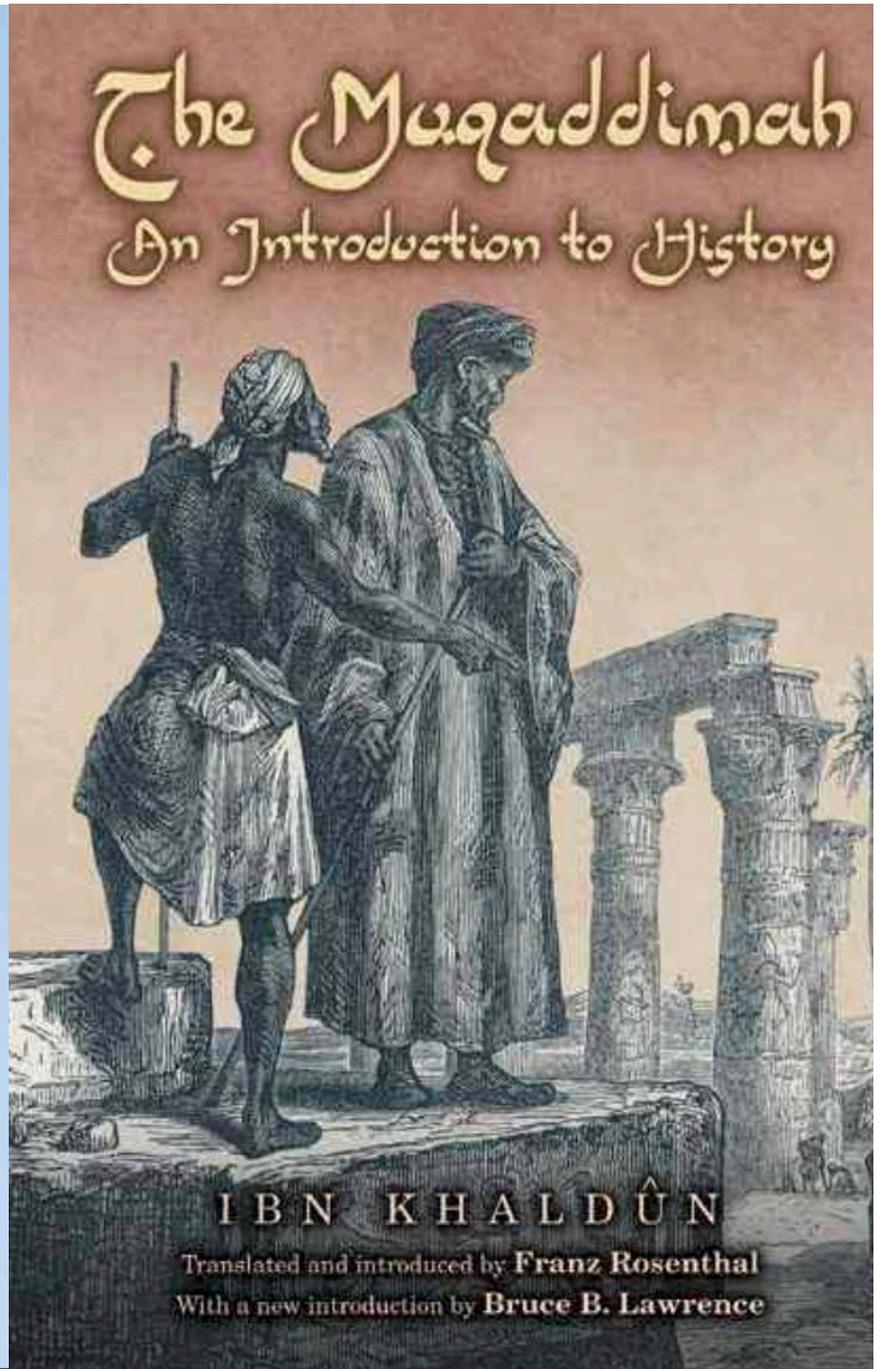


First part: the ambition of a “universal history”

- Herodotus (5th century BCE).
 - Ibn Khaldun (14th century)
 - Bernard de Mandeville (end 17th, beginning 18th century)
 - Adam Smith (18th century: TMS 1759, WN 1776)
 - Edward Gibbon (18th century, HDFRE 1776-89)
-

PENGUIN CLASSICS
HERODOTUS
THE HISTORIES





THE
F A B L E
OF THE
B E E S:

OR,
Private Vices, Publick Benefits.

By
BERNARD MANDEVILLE.

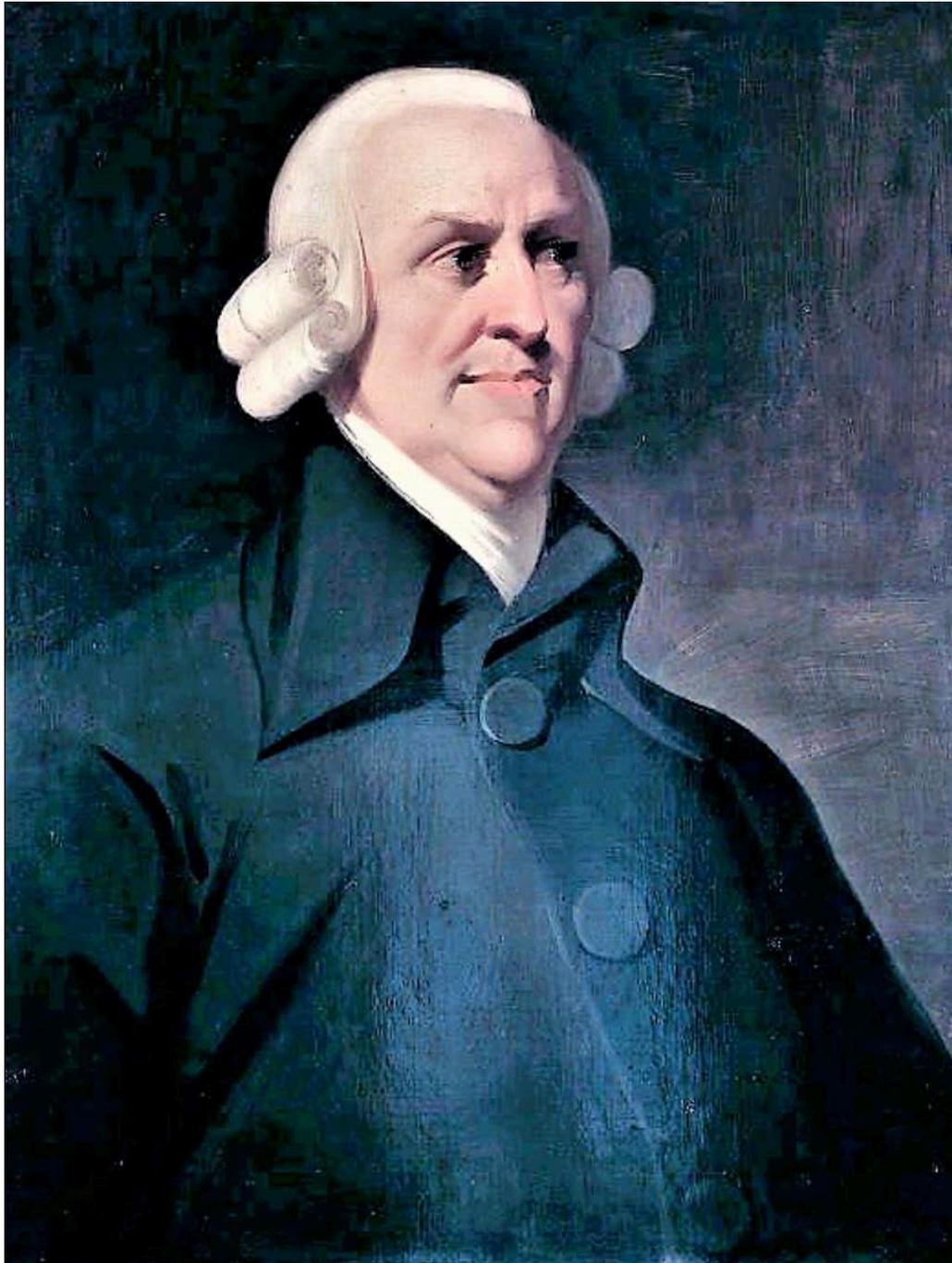
With a Commentary
Critical, Historical, and Explanatory by
F. B. KAYE

The FIRST VOLUME

OXFORD:
At the Clarendon Press
M D C C C C X X I V



Pride and vanity have built more hospitals than all the virtues together,



Adam Smith

An Inquiry into
the Nature and Causes of
**The Wealth of
Nations**



Edited and with an
Introduction, Notes, Marginal Summary, and Index
by EDWIN CANNAN

With a new Preface by George J. Stigler



EDWARD GIBBON
FROM THE PAINTING BY HENRY WALTON IN THE NATIONAL PORTRAIT GALLERY

THE HISTORY
OF THE
DECLINE AND FALL OF THE
ROMAN EMPIRE

BY
EDWARD GIBBON

EDITED
WITH INTRODUCTION, NOTES, AND APPENDICES

BY
J. B. BURY, D.LITT., LL.D.
CORRESPONDING MEMBER OF THE IMPERIAL ACADEMY OF SCIENCES, ST. PETERSBURG
FELLOW OF KING'S COLLEGE AND REGIUS PROFESSOR OF MODERN HISTORY
IN THE UNIVERSITY OF CAMBRIDGE

IN SEVEN VOLUMES
VOLUME I

WITH TWENTY ILLUSTRATIONS AND MAP



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LONDON

Second Edition

Letter from
Edward
Gibbon
to Adam
Smith, 26th
November
1777

Dear Sir

Among the strange reports which are every day circulated in this wide town, I heard one to-day so very extraordinary, that I know not how to give credit to it. I was informed that a place of Commissioner of the Customs in Scotland had been given to a Philosopher who for his own glory and for the benefit of mankind had enlightened the world by the most profound and systematic treatise on the great objects of trade and revenue which had ever been published in any age or in any Country. But, as I was told at the same time that this Philosopher was my particular friend, I found myself very forcibly inclined to believe, what I most sincerely wished and desired

The partial and global perspectives: Adam Smith on the social utility of religion

That the terrors of religion should thus enforce the natural sense of duty, was of too much importance to the happiness of mankind, for nature to leave it dependent upon the slowness and uncertainty of philosophical researches – *The Theory of Moral Sentiments*, Part III, Chapter V

Echoed by Edward Gibbon?

“The various modes of worship, which prevailed in the Roman world, were all considered by the people, as equally true; by the philosopher, as equally false; and by the magistrate, as equally useful. And thus toleration produced not only mutual indulgence, but even religious concord.” *History of the Decline and Fall of the Roman Empire*.

New directions: Adam Smith on incentives, the division of labor, and the similarity of people of all social ranks

It is not from the benevolence of the butcher, the brewer, or the baker, that we can expect our dinner, but from their regard to their own interest.....The difference of natural talents in different men is, in reality, much less than we are aware of; and the very different genius which appears to distinguish men of different professions, when grown up to maturity, is not upon many occasions so much the cause as the effect of the division of labour. The difference between the most dissimilar characters, between a philosopher and a common street porter, for example, seems to arise not so much from nature as from habit, custom, and education. When they came into the world, and for the first six or eight years of their existence, they were perhaps very much alike, and neither their parents nor playfellows could perceive any remarkable difference. About that age, or soon after, they come to be employed in very different occupations. The difference of talents comes then to be taken notice of, and widens by degrees, till at last the vanity of the philosopher is willing to acknowledge scarce any resemblance. But without the disposition to truck, barter, and exchange, every man must have procured to himself every necessary and conveniency of life which he wanted. All must have had the same duties to perform, and the same work to do, and there could have been no such difference of employment as could alone give occasion to any great difference of talents – *Wealth of Nations*, Book I, Chapter II

What look like differences of theology boil down in the end to differences in incentives:

The [clergy] may either depend altogether for their subsistence upon the voluntary contributions of their hearers; or they may derive it from some other fund to which the law of their country may entitle them; such as a landed estate, a tythe or land tax, an established salary or stipend. Their exertion, their zeal and industry, are likely to be much greater in the former situation than in the latter. In this respect the teachers of new religions have always had a considerable advantage in attacking those ancient and established systems of which the clergy, reposing themselves upon their benefices, had neglected to keep up the fervour of faith and devotion in the great body of the people; and having given themselves up to indolence, were become altogether incapable of making any vigorous exertion in defence even of their own establishment. The clergy of an established and well-endowed religion frequently become men of learning and elegance, who possess all the virtues of gentlemen, or which can recommend them to the esteem of gentlemen; but they are apt gradually to lose the qualities, both good and bad, which gave them authority and influence with the inferior ranks of people, and which had perhaps been the original causes of the success and establishment of their religion. – *Wealth of Nations*, book V, chapter I.



Second part: the complex nature of sympathy

- The coexistence of selfishness and sympathy:
 - Smith's criticism of Mandeville.
 - The indirect benefits of benevolence.
 - Even love of praise is tempered by the need for validation.
 - The by-products of ignoble motives and the invisible hand.
 - The impartial spectator is a fiction: those who try to improve society are real people with real (and fickle) motives.
-

Adam Smith on Mandeville's cynicism:

It is the great fallacy of Dr Mandeville's book to represent every passion as wholly vicious, which is so in any degree and in any direction.... But how destructive soever this system may appear, it could never have imposed upon so great a number of persons, nor have occasioned so general an alarm among those who are the friends of better principles, had it not in some respects bordered upon the truth –
The Theory of Moral Sentiments, Chapter Part VII, Chapter IV.

Adam Smith on the indirect way in which benevolence may benefit the benevolent person

No benevolent man ever lost altogether the fruits of his benevolence. If he does not always gather them from the persons from whom he ought to have gathered them, he seldom fails to gather them, and with a tenfold increase, from other people. Kindness is the parent of kindness; and if to be beloved by our brethren be the great object of our ambition, the surest way of obtaining it is, by our conduct to show that we really love them – *The Theory of Moral Sentiments*, Part VI, Chapter I

Adam Smith on love, praise..

Man naturally desires, not only to be loved, but to be lovely; or to be that thing which is the natural and proper object of love. He naturally dreads, not only to be hated, but to be hateful; or to be that thing which is the natural and proper object of hatred. He desires, not only praise, but praise-worthiness – *The Theory of Moral Sentiments*, Part III, Chapter II



Adam Smith on the by-products of ignoble motives:

This disposition to admire, and almost to worship, the rich and the powerful, and to despise, or, at least, to neglect persons of poor and mean condition, though necessary both to establish and to maintain the distinction of ranks and the order of society, is, at the same time, the great and most universal cause of the corruption of our moral sentiments – *The Theory of Moral*

Sentiments, Chapter Part I, Chapter III.



The vanity of ambition:

What the favourite of the king of Epirus said to his master, may be applied to men in all the ordinary situations of human life. When the King had recounted to him, in their proper order, all the conquests which he proposed to make, and had come to the last of them; And what does your Majesty propose to do then? said the Favourite. –I propose then, said the King, to enjoy myself with my friends, and endeavour to be good company over a bottle. –And what hinders your Majesty from doing so now? – *The Theory of Moral Sentiments*, Chapter Part III, Chapter III.

But its social utility nevertheless:

And it is well that nature imposes upon us in this manner. It is this deception which rouses and keeps in continual motion the industry of mankind. It is this which first prompted them to cultivate the ground, to build houses, to found cities and commonwealths, and to invent and improve all the sciences and arts, which ennoble and embellish human life; which have entirely changed the whole face of the globe – *The Theory of Moral Sentiments*, Chapter Part IV, Chapter I.

The first appearance of the invisible hand:

The rich only select from the heap what is most precious and agreeable. They consume little more than the poor, and in spite of their natural selfishness and rapacity, though they mean only their own conveniency... are led by an invisible hand to make nearly the same distribution of the necessaries of life, which would have been made, had the earth been divided into equal portions among all its inhabitants, and thus without intending it, without knowing it, advance the interest of the society – *The Theory of Moral*

Sentiments, Part IV, Chapter I



The impartial spectator is a fiction: in reality, those who try to improve society are real people with real motives

From a certain spirit of system, however, from a certain love of art and contrivance, we sometimes seem to value the means more than the end, and to be eager to promote the happiness of our fellow-creatures, rather from a view to perfect and improve a certain beautiful and orderly system, than from any immediate sense or feeling of what they either suffer or enjoy – *The Theory of Moral Sentiments*, Part IV, Chapter I

Adam Smith on the delusions of the central planner:

He seems to imagine that he can arrange the different members of a great society with as much ease as the hand arranges the different pieces upon a chess-board. He does not consider that the pieces upon the chess-board have no other principle of motion besides that which the hand impresses upon them; but that, in the great chess-board of human society, every single piece has a principle of motion of its own, altogether different from that which the legislature might chuse to impress upon it – *The Theory of*

Moral Sentiments, Part VI, Chapter II



Reconciliation of the two Adam Smiths:

- The Smith who wrote TMS and the one who wrote WN are recognizably the same thinker.
- Self-interest and sympathy coexist inside every person:
 - Self-interest is tempered by a concern not just for what others think but for what they ought to think.
 - The impartial spectator is a fiction; in reality he struggles against self-serving and self-aggrandizing desires.
- The tension between the particular and general perspective on human society is as present in TMS as in WN; it was inherited from the tradition of universal history.



A parenthesis on anachronism...

- Beware of anachronism:
- Smith sometimes seems astonishingly modern.
- But he was a man of his time.
- Compare his views on slavery, which seem very modern, with his views on sex and gender, which are very much those of an 18th century bachelor gentleman.



Adam Smith indignant at slavery:

There is not a negro from the coast of Africa who does not, in this respect, possess a degree of magnanimity which the soul of his sordid master is too often scarce capable of conceiving. Fortune never exerted more cruelly her empire over mankind, than when she subjected those nations of heroes to the refuse of the jails of Europe, to wretches who possess the virtues neither of the countries which they come from, nor of those which they go to, and whose levity, brutality, and baseness, so justly expose them to the contempt of the vanquished – *The Theory of Moral Sentiments*, Part V, Chapter II

Adam Smith the unreconstructed chauvinist...

Breach of chastity dishonours irretrievably. No circumstances, no sollicitation can excuse it; no sorrow, no repentance atone for it. We are so nice in this respect that even a rape dishonours, and the innocence of the mind cannot, in our imagination, wash out the pollution of the body – *The Theory of Moral Sentiments*, Part VII, Chapter IV

Back to Heilbroner, and the “new professordom”

- Heilbroner writes of “The Victorian World and the Underworld of Economics”.
- The “new professordom” was exemplified by Francis Edgworth, Johann Heinrich von Thünen, Leon Walras, Stanley Jevons, John Bates Clark, Alfred Marshall.
- Heilbroner was scathing about what he called the new professordom’s “attempt to dehumanize political economy” (p.175).
- He contrasted it with the “underworld” of Bernard Mandeville, Frédéric Bastiat, Henry George, John Hobson, which flourished “as a counterpart to this pale world of equations” (p.177).
- Then later with the “savage society” of Thorstein Veblen and the “heresies” of John Maynard Keynes.

What was Heilbroner's criticism exactly?

- Five possibilities – at various points he accuses the professordom of:
 - Abstraction.
 - Mathematization and quantification.
 - Reduction of the domain of study to what Marshall called “the ordinary business of life”... that “shuns many political issues, which the practical man cannot ignore” (p.209).
 - Focus on “the Individual, whose calculations not only symbolize the workings of the market system but are in fact the rock on which the economy itself ultimately rests” (p. 209).
 - Aloofness from the big questions of society – unemployment, war, poverty etc.

 - Ironically, in the 20th century these would no longer be uniformly found together:
 - Lionel Robbins (1936) defined economics very abstractly as the study of “the allocation of scarce resources among competing ends”, an insight used by Gary Becker among others to study phenomena well outside “the ordinary business of life”, such as marriage, crime, addiction.
-

Textbooks in the 20th Century

- Bowles and Carlin (JEL 2019) compare the content of Marshall's *Principles*, Samuelson's *Economics*, Mankiw's *Principles of Economics*, Krugman and Wells' *Economics*, plus their own open access CORE text.
- They argue that
 - “the content of our introductory economics courses now fails to provide tools adequate to address pressing societal and economic problems”
 - “these tools are available (indeed widely taught in PhD programs)”
 - “they can be made accessible, engaging and be successfully taught to first year students”.
- They use Bayesian topic modeling to generate 100 core economic topics from 27,436 research papers in top-5 plus REStat from 1900-2014, then compare the weighting of these topics in the various textbooks.

Samuelson's motivation:

- “Today the non-specialist in physics deserves and expects to learn about atomic energy and nuclear structure in his first year of study, rather than remain bogged down in elementary experiments on falling bodies and heat calorimetry. Why then should teachers of economics withhold from the first-year course the really interesting and vital problems of over-all economic policy?”
 - The political health of a democracy is tied up in a crucial way with the successful maintenance of stable high employment and living opportunities. It is not too much to say that the widespread creation of dictatorships and the resulting World War II stemmed in no small measure from the world's failure to meet this basic economic problem adequately.
-

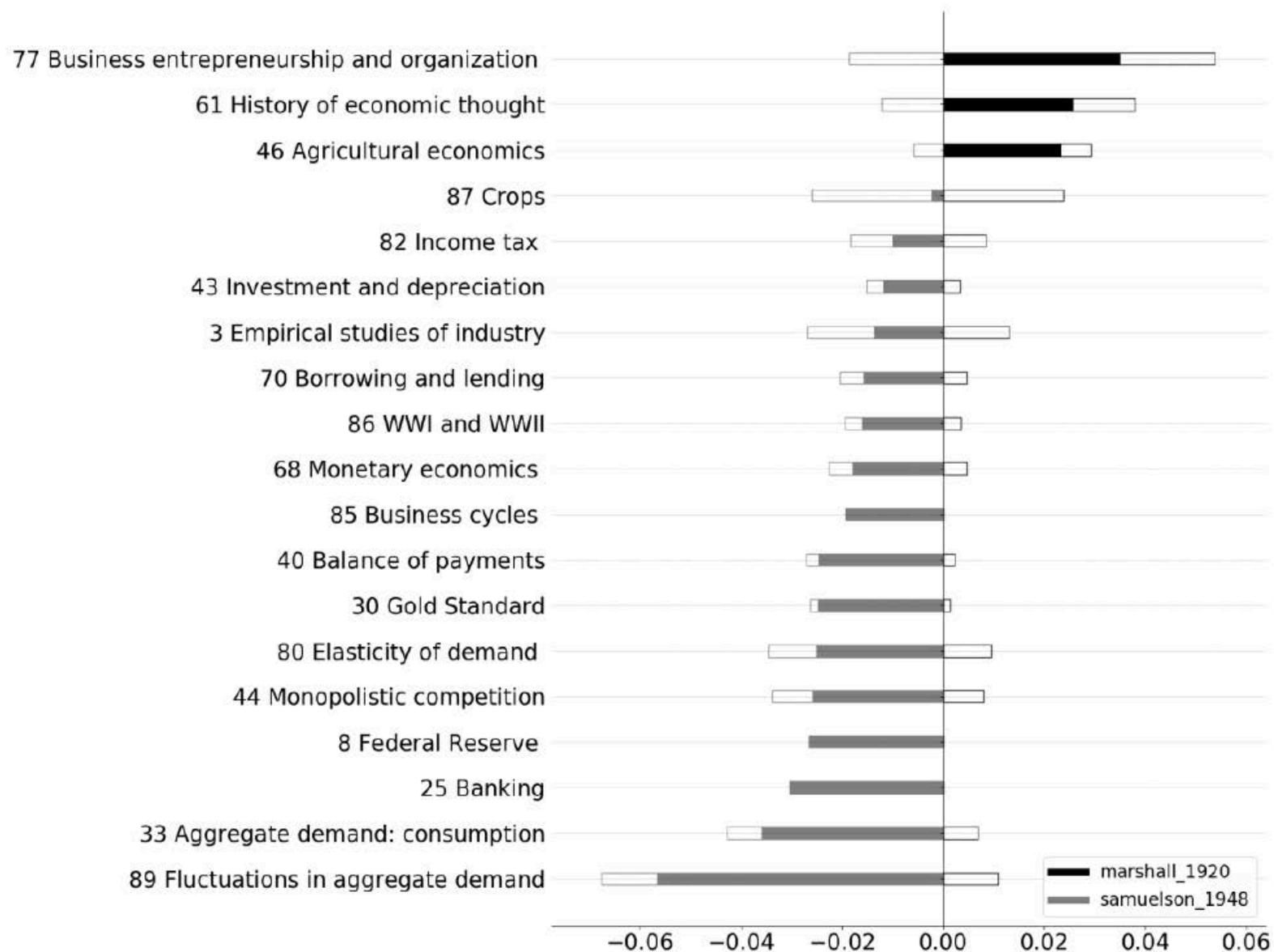


Figure 4: Comparison of content in Samuelson 1948 and Marshall 1890. A topic is included if it has a weight not less than 0.015 in at least one of the texts. Three topics in which the token

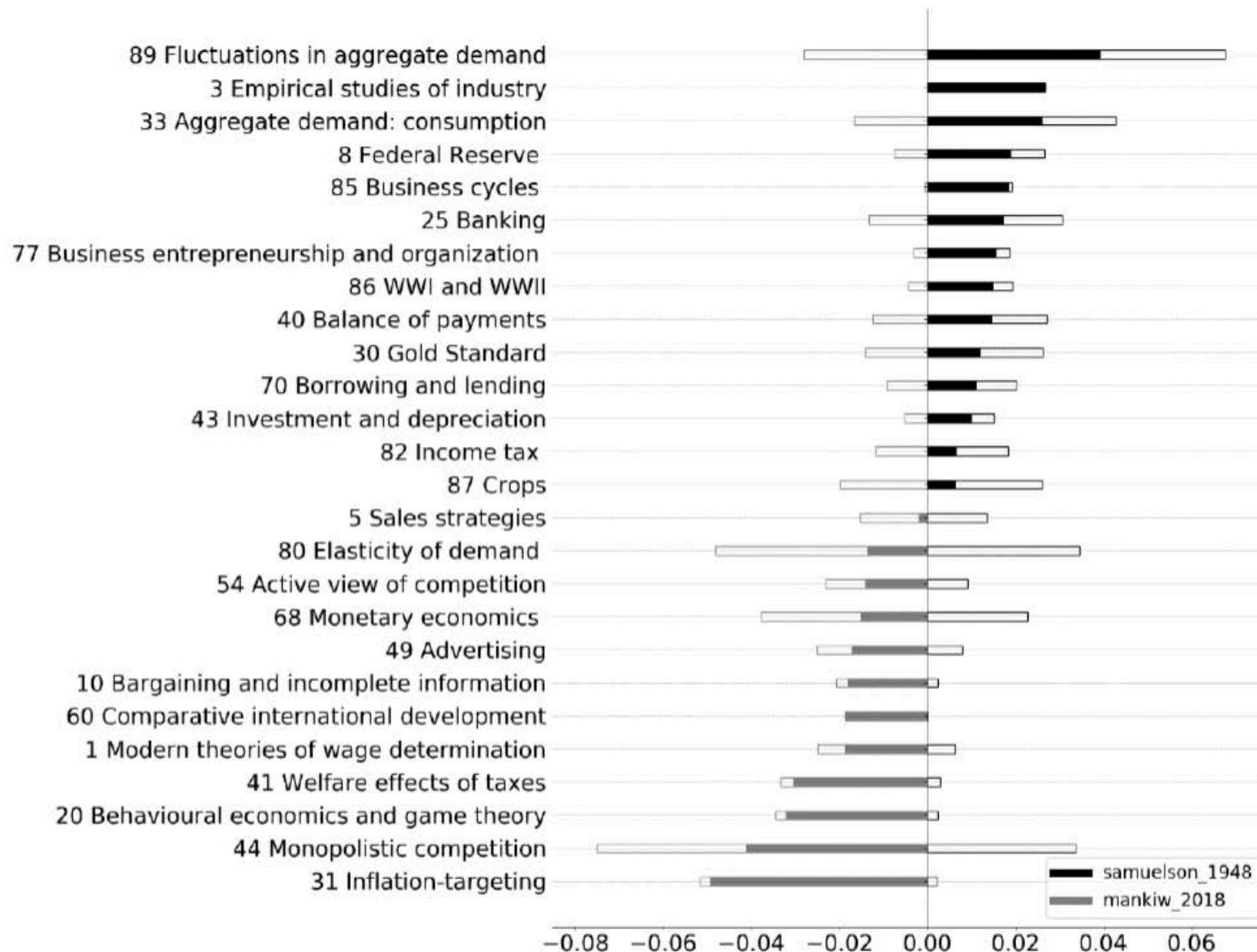


Figure 5: A topic comparison of Samuelson 1948 and Mankiw 2018. As in the earlier figure, the length of each outline bar measures the importance of that topic for the two texts. The solid bars show the difference in the weight on the topic between the two texts.

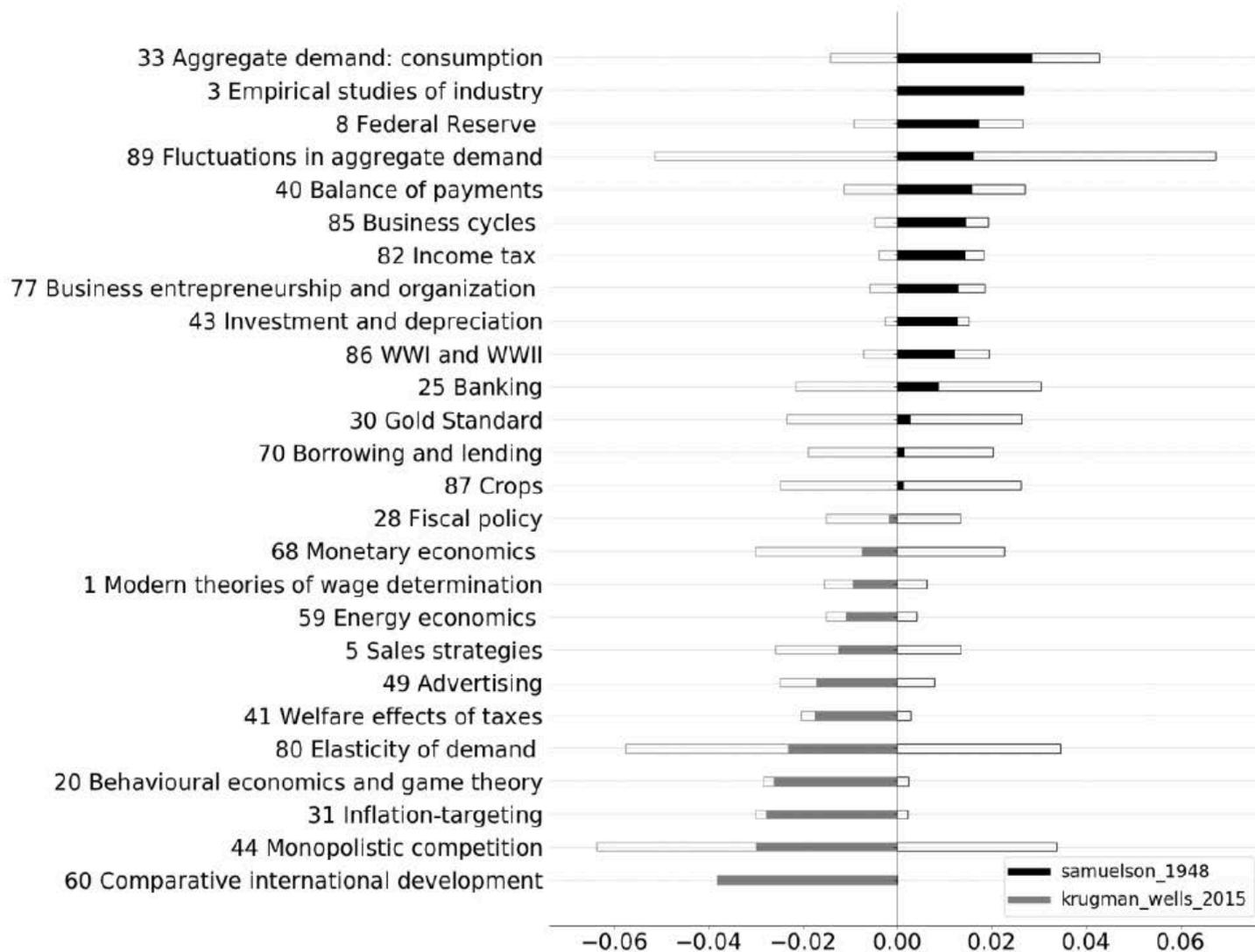


Figure 6: A topic comparison of Samuelson 1948 and Krugman and Wells, 2015. As in the earlier figures, the length of each outline bar measures the importance of that topic for the two texts. The solid bars show the difference in the weight on the topic between the two texts.

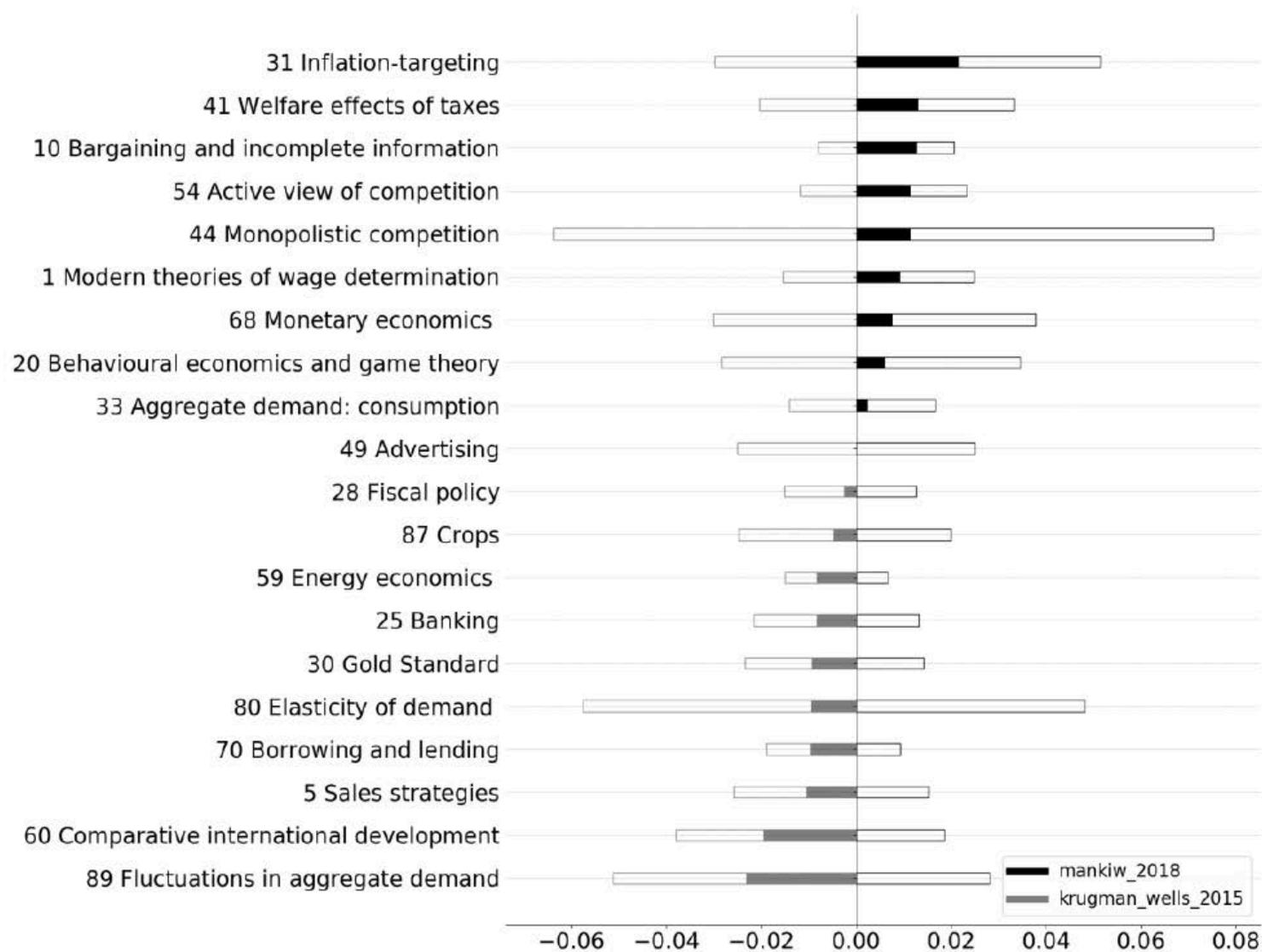


Figure 7: A topic comparison of Mankiw 2018 and Krugman and Wells, 2015. As in the earlier figures, the length of each outline bar measures the importance of that topic for the two texts. The solid bars show the difference in the weight on the topic between the two texts.

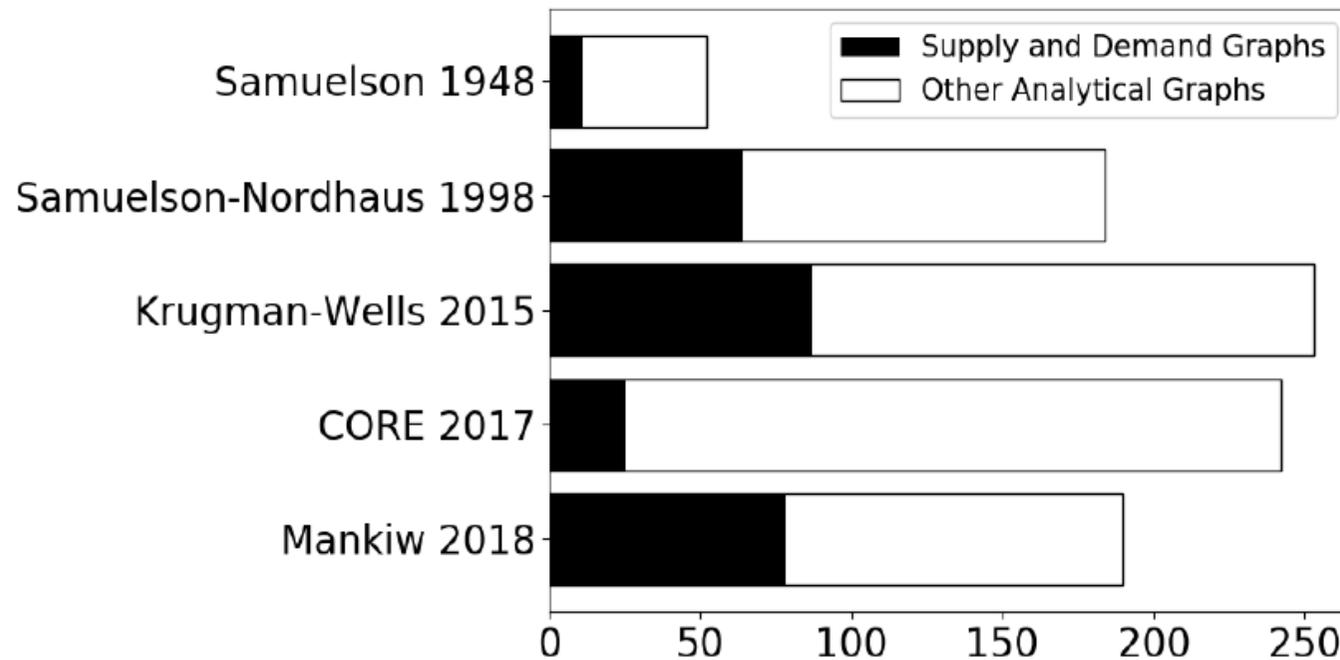


Figure 10: Supply and Demand Figures as a Fraction of all Analytical Figures in Texts. A figure is counted if there is both a supply and a demand curve (hence depicting a competitive market) or if the AD/AS model is shown. If several graphs are simply about building up the final figure, this counts as one and if for example there are two panels – one with the market for apples and the other for apple-pickers, this counts as two. The number of AD/AS figures in the texts (in the above order) is: 0, 16, 9, 16 and 0.



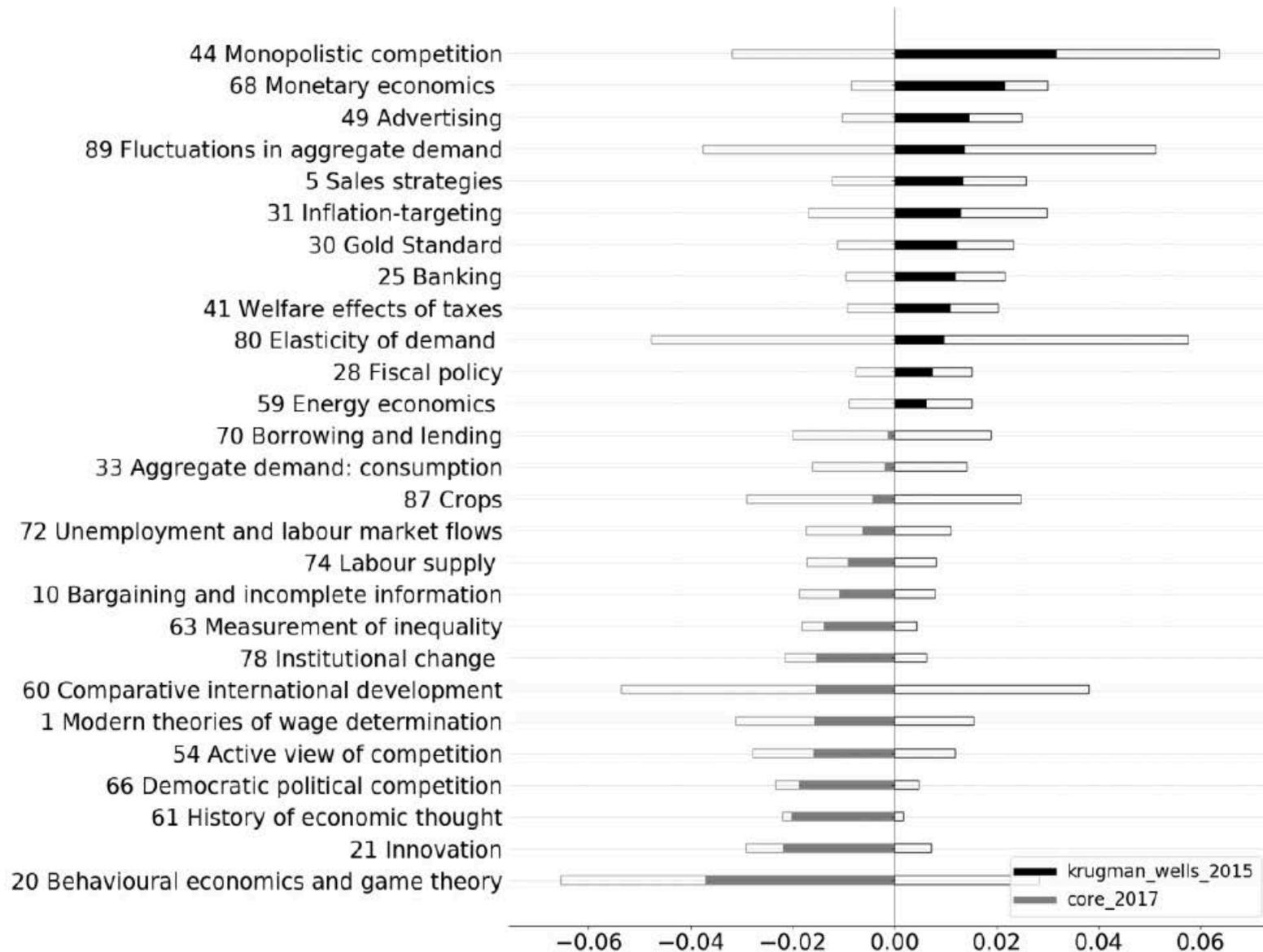


Figure 11: A topic comparison of CORE 2018 and Krugman and Wells, 2015. As in the earlier figures, the length of each outline bar measures the importance of that topic for the two texts. The solid bars show the difference in the weight on the topic between the two texts.

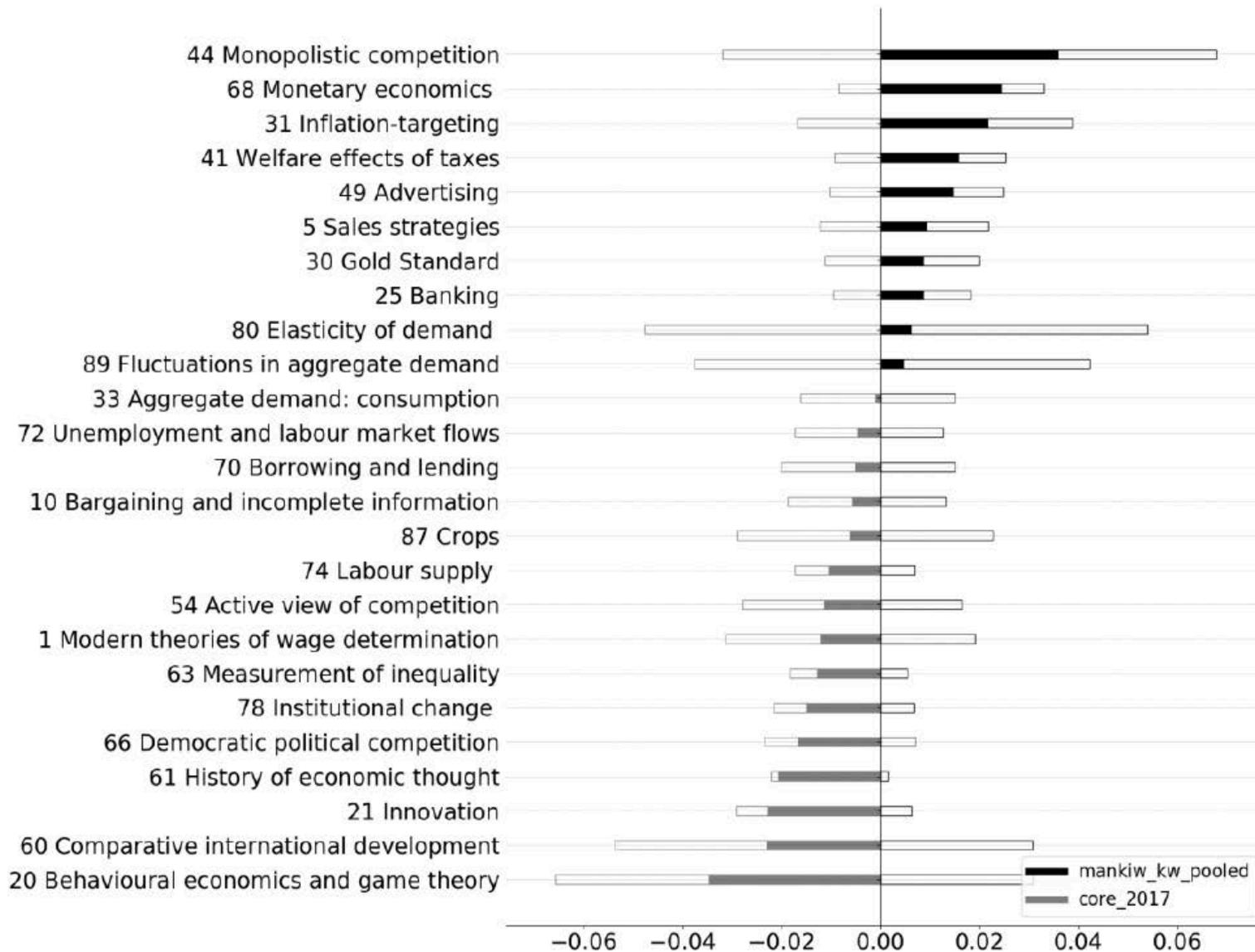


Figure 12: A topic comparison of CORE 2018 and Krugman and Mankiw 2018. As in the earlier figures, the length of each outline bar measures the importance of that topic for the two texts. The solid bars show the difference in the weight on the topic between the two texts.

Summary: the development of economics as a discipline

- The standard view of the origins of economics as a discipline takes Adam Smith to be doing something very new, and very different from the work of previous scholars and those in other disciplines such as history.
 - We can now take a more nuanced view of this, and see the professionalisation of economics as taking place in different dimensions and as being linked to the rise of universities as institutions in society.
 - Smith was a great innovator but in substantive theory rather than his vision of the proper domain of economics, which was much broader, more political and behavioral, than subsequently became the standard.
 - The university discipline of economics passed through a narrow funnel in the 19th and 20th centuries, from which it only began to emerge in the last quarter of the 20th century, returning towards its roots in “universal history”.
-

The rapprochement of economics and other social sciences in the late 20th and early 21st centuries - five domains:

-
- The endogenous treatment of political institutions
 - The public choice school and regulatory capture
 - Social capital, institutions as a constraint on growth and development
 - The development of game theory in economics and biology
 - Evolutionary stable strategies and Nash equilibria
 - Kin selection, reciprocal altruism and the problem of cooperation
 - The “evolutionary turn” in anthropology and psychology
 - The “rational choice” approach to sociology: crime, religion, addiction, networks
 - Behavioral economics as a beneficiary of all of the above: “heuristics and biases”, identity, social preferences, personality
-

The rapprochement of economics and other social sciences in the late 20th and early 21st centuries - five domains (II):

-
- In each of these domains economics and other social science disciplines found a common set of questions of interest, and in the process began to converge to some degree in their methods.
 - This process has also enabled us to use empirical evidence from one discipline to inform us about the plausibility of hypotheses in another.
 - That doesn't mean that human societies are just like other animal societies (part of what the comparison forces us to do is to think about how and why human societies are different).
 - But it does mean that there is no longer any reason to ignore important work done in one domain just because the people who performed it were working in different university departments.
-