PHIL 721 Section 001 - Advanced Seminar

Philosophy of Economics
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Wednesday, 4:30-7:10pm. Classroom: Robinson B, Room 442
Office Hours: Wednesday 12:30-2:00; Thursday 11:30-1:00 and by appointment.
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This is a course in philosophy not economics. Philosophers are interested in economics for many reasons two of which will be studied here. First, economics claims as a science to represent, explain, predict, or help to manage facts about the world. Philosophers of science dig into such claims and question whether and how models, constructs, theories, laws, metaphors, useful fictions, and other concepts associated with economics help us to understand our experience. Second, although many economists would deny it, economic research is chock-a-block with values such as “cost” “benefit,” “welfare,” “efficiency,” and “wealth.” Philosophers want to know how economists understand and measure these values and whether they make sense in terms of broadly accepted social norms and goals. This course asks, in other words, whether and how economic science can tell us anything about facts or about values. Since these are philosophical questions, we shall approach them – as many economists themselves have done -- through philosophical analysis.

This course will follow a format of structured discussion; your participation is therefore necessary. Everyone is expected to do all the readings before coming to class and to join in the class conversation about them. *(This will require you to print out and annotate the readings from Blackboard before each class; if this presents difficulties, please let me know.)* All of the readings have been (or will soon be) made available on Blackboard. In many instances I have high-lighted some of the most important passages. (Remove these highlights if they annoy you). There are also recommended readings.

**Assessment**

There will be 2 midterm essay exams, each taking half a class period, on the readings and discussions up to that time. The midterm exams are scheduled for October 12 and November 16.

While these are closed-book exams, I will distribute a list of several questions at least a week in advance; some choice among these will appear as exam questions. There is a final paper but no final exam. The classes begin August 31st and end on December 7th. The final paper, which should be about 20 pages, is due at the end of exam period, December 21.

It is crucial that your paper go through at least two preliminary drafts. The first, which could be a prospectus, a paper proposal, or something more elaborate, is due November 9. A substantial first draft of the paper is due November 30. There is no limit on the number of drafts you can submit and thus the number of comments and suggestions you will receive as a result.

Other Information:

ACADEMIC INTEGRITY

GMU is an Honor Code university; please see the University Catalog for a full description of the code and the honor committee process. The principle of academic integrity is taken very seriously and violations are treated gravely. What does academic integrity mean in this course? Essentially this: when you are responsible for a task, you will perform that task. When you rely on someone else’s work in an aspect of the performance of that task, you will give full credit in the proper, accepted form. Another aspect of academic integrity is the free play of ideas. Vigorous discussion and debate are encouraged in this course, with the firm expectation that all aspects of the class will be conducted with civility and respect for differing ideas, perspectives, and traditions. When in doubt (of any kind) please ask for guidance and clarification.

GMU EMAIL ACCOUNTS
Students must use their Mason email accounts—either the existing “MEMO” system or a new “MASONLIVE” account to receive important University information, including messages related to this class. See http://masonlive.gmu.edu for more information.

OFFICE OF DISABILITY SERVICES
If you are a student with a disability and you need academic accommodations, please see me and contact the Office of Disability Services (ODS) at 993-2474. All academic accommodations must be arranged through the ODS. http://ods.gmu.edu

OTHER USEFUL CAMPUS RESOURCES:

WRITING CENTER: A114 Robinson Hall; (703) 993-1200; http://writingcenter.gmu.edu

UNIVERSITY LIBRARIES “Ask a Librarian”
http://library.gmu.edu/mudge/IM/IMRef.html

COUNSELING AND PSYCHOLOGICAL SERVICES (CAPS): (703) 993-2380; http://caps.gmu.edu

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PART I: ECONOMICS AND SCIENCE

Week 1: Introduction (August 31)

(These are very general readings which you should complete as soon as possible)


“Economics is what economists do.” Statement attributed to Jacob Viner.


“there is no way to do economics if one is not willing to simplify drastically and abstract from many complications. How much simplification, idealization, and abstraction is legitimate?” p. 7.

Week 2: John Stuart Mill and Lionel Robbins on confirmation in economics. (Sept. 07)


The science which traces the laws of such of the phenomena of society as arise from the combined operations of mankind for the production of wealth, in so far as those phenomena are not modified by the pursuit of any other object. (p. 6)


The propositions of economic theory, like all scientific theory, are obviously deductions from a series of postulates. ... The main postulate of the theory of value is the fact that individuals can arrange their preferences in an order, and in fact do so. The main postulate of the theory of production is the fact that there are [sic] more than one factor of production. The main postulate of the theory of dynamics is the fact that we are not certain regarding future scarcities. These are not postulates the existence of whose counterpart in reality admits of extensive dispute once their nature is fully realised. We do not need controlled experiments to establish their validity: they are so much the stuff of our everyday experience that they have only to be stated to be recognized as obvious. (p. 79 in 1945 edition)


we ought at least to recognise as fundamental a positive science of political economy which is concerned purely with what is, and which seeks to determine economic laws.
Week 3: Milton Friedman and Critics: Positivism in Economics (Sept. 14)


Positive economics is in principle independent of any particular ethical position or normative judgments. As Keynes says, it deals with "what is," not with "what ought to be." Its task is to provide a system of generalizations that can be used to make correct predictions about the consequences of any change in circumstances. Its performance is to be judged by the precision, scope, and conformity with experience of the predictions it yields. In short, positive economics is, or can be, an "objective" science, in precisely the same sense as any of the physical sciences.

An obvious and not unimportant example is minimum-wage legislation.

“[The academic economist] must for instance analyse the methods which people are tempted to take for securing a high minimum wage . . . and must show which of them will have indirect effects that will cause workingmen as a whole a loss greater than the benefit. . . . ordinary people do not see that the means most commonly advocated . . . would impoverish all” (Alfred Marshall, “The Old Generation of Economists and the New." Quarterly Journal of Economics 11.2:115–35 (1897), p. 128).

“If law or opinion succeeds in fixing wages above this [competitive] rate, some laborers are kept out of employment; as it is not the intentions of the philanthropists that these should starve, they must be provided for.” (John Stuart Mill, Principles of Political Economy with Some of Their Applications to Social Philosophy. Boston: Little & Brown 1848, p. 432)


there is little evidence . . . that minimum wage increases reduce employment.


It is far more important to know whether they [deviations of observation from theory] are significant in the sense that the approximation of theory to reality is beyond the limits of our tolerance.


the freedom of master and employee to contract with each other in relation to their employment cannot be prohibited or interfered with without violating the Constitution.

In particular, minimum wage research has come to be seen as a test of the applicability of neoclassical price theory to the determination of wages and employment.


Minimum wages: A venerable topic in economics and area of ongoing controversy

Week 4: Falsification in Economics (September 21)

Note: In his syllabus for the Philosophy of Economics course taught at the University of Wisconsin, Dan Hausman states: “Warning! Philosophy challenges complacency. It is hard to know what the truth is concerning hard questions like the ones we will be addressing this semester.” This is especially true of understanding the conditions under which the qualifier “all else being equal” turns a general statement into a vacuity.


I wished to distinguish between science and pseudo-science; knowing very well that science often errs, and that pseudoscience may happen to stumble on the truth.

“the fact is that falsification is seldom if ever practiced in economics. . . [The question is whether it should be practiced” – D. Wade Hands “Popper and Lakatos in Economic Methodology” (1993).


Popper replaced the central problem of classical rationality, the old problem of foundations, with the new problem of fallible-critical growth, and started to elaborate objective standards of this growth.


The gap between model world and real world can be filled only by inductive inference, and we can have more confidence in such inferences, the more credible the model is as an account of what could have been true.

Nancy Cartwright, “If No capacities then No Credible Worlds’, Erkenntnis, 70 (1), 45-58.

Economics has very few uncontroversial principles at its disposal. Its models must do a lot with a little.
Week 5.  *Ceteris Paribus*  (September 28)


When Mill enunciates the "psychological law" "that a greater gain is preferred to a smaller", he is not claiming that people always prefer greater gains, but that this is one motivational "force" that often predominates. Economists tell us how agents behave in the absence of various complications.

[Note: The following readings are very difficult. Have a go at them. Part of the purpose is to illustrate the difficulty of understanding how models, theories, and assumptions in economics are justified.]

John Earman, John Roberts, and Sheldon Smith, “Ceteris Paribus Lost,” *Erkenntnis* 57(2002): 281-301.  [It helps to start with the tobacco example at the end of the paper]

In order for a hypothesis to be testable, it must lead us to some prediction. The prediction may be statistical in character, and in general it will depend on a set of auxiliary hypotheses. Even when these important qualifications have been added, CP law statements still fail to make any testable predictions.


Here’s what I think happens. We have seen a vast number of cases of forces at work to which we have tried to fit Newton’s second law and over time we have established very strong rules of thumb about what can make trouble for it. That is, we have learned from a lot of experience what kinds of things might interfere with the operation of the force. That’s what we control for.

Week 6.  Economics in Crisis (October 5)


Or perhaps economics will remain a discipline that forgets most of what it once knew and allows itself to be continually distracted, confused, and in denial.


The fundamental misconception here lies in the understanding of what ‘the economy’ is.

The peculiar character of the problem of a rational economic order is determined precisely by the fact that the knowledge of the circumstances of which we must make use never exists in concentrated or integrated form but solely as the dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess.

Recommended:


The statement that, if people know everything, they are in equilibrium is true simply because that is how we define equilibrium.


Human choice was reduced to an exercise in constrained optimisation, and the force of competition was redefined as a state of affairs rather than a set of active engagements.

PART II -- LAW, ECONOMICS, AND ETHICS

Week 7. October 12. First Midterm Exam (first half of class period).

Reading for second half of class:


In all cases, therefore, where a certain policy leads to an increase in physical productivity, and thus of aggregate real income, the economist's case for the policy is quite unaffected by the question of the comparability of individual satisfactions; since in all such cases it is possible to make everybody better off than before, or at any rate to make some people better off without making anybody worse off.

Recommended – quick look:


[In Third-World countries] US wheat surpluses made imports an attractive alternative to the modernization of the domestic food sector.

To see how far some economists have taken the “compensation test” as a measure of value, look at: Zerbe Jr., Richard O, Yoram Bauman, and Aaron Finkle, 2005. “An

A logical extension or clarification of KH requires including all goods for which there is a WTP.

**Week 8. Should Preferences Count? (October 19)**


Incoherence of the preference sovereignty norm implies the radical conclusion that welfare economics does not have a positive marginal product in judging welfare or making social decisions.

Amartya K. Sen, *Rational Fools: A Critique of the Behavioral Foundations of Economic Theory* Philosophy & Public Affairs Vol. 6, No. 4 (Summer, 1977), pp. 317-344. Behavior, it appears, is to be explained in terms of preferences, which are in turn defined only by behavior. Not surprisingly, excursions into circularities have been frequent.

The characteristic of commitment with which I am most concerned here is the fact that it drives a wedge between personal choice and personal welfare, and much of traditional economic theory relies on the identity of the two.


Yet it is obvious that people’s preferences are not always self-interested and that false beliefs may lead people to prefer what is worse for them even when people are self-interested. So welfare is not preference satisfaction, and hence it appears that cost-benefit analysis and welfare economics in general rely on a mistaken theory of wellbeing.

**Week 9. Social Costs and Property Rights (October 26).**


In a world in which there are costs of rearranging the rights established by the legal system, the courts, in cases relating to nuisance, are, in effect, making a decision on the economic problem and determining how resources are to be employed.


Whenever society chooses an initial entitlement it must also determine whether to protect the entitlement by property rules, by liability rules, or by rules of inalienability.

Why should the trial court have allowed the cement company, in empirical effect, to buy up its neighbors?

Week 10. Social Costs continued. (November 2)


Transaction costs (including problems of rationality and knowledge), no less than existing technology, define what is currently achievable in any society—the Pareto frontier.

Week 11. Cost-Benefit Analysis (I) (November 9)

[FIRST DRAFTS or at least a perspective of papers are due.]


When the existence of a grand scenic wonder or a unique and fragile ecosystem is involved, its preservation and continued availability are a significant part of the real income of many individuals.

Larry Ruff, The Economic Common Sense of Pollution,” *The Public Interest, 19* (Spring 1970); read excerpts at: [http://www.terry.uga.edu/~satkinso/2100/econcommonsense.doc](http://www.terry.uga.edu/~satkinso/2100/econcommonsense.doc)

Once the prices are set, polluters can adjust to them in any way they choose. Because they act on self-interest they will reduce pollution by every means possible up to the point where further reduction would cost more than the price.


Externalities Run Wild


A fundamental problem with the concept of market failure, as economists occasionally recognize, is that it describes a situation that exists everywhere

Recommended but difficult:

the rhetoric of Kaldor-Hicks is so thoroughly manipulable that liberals and conservatives can pursue agendas of these kinds within its strictures... [The effect is] supportive of liberalism and conservatism together, seen as a bloc in opposition to more left and right wing positions. What the liberal and conservative members of the centrist bloc have in common is moderation, statism and rationalism.

Week 12. Cost-Benefit Analysis II (November 16)

[Second Midterm Exam (first half of class period)].

Reading for second half of class:


Rich and poor alike have an interest in making the economic pie as large as possible. Any policy that passes the cost-benefit test makes the economic pie larger. And when the pie is larger, everyone can have a larger slice.

[Question: What does “the economic pie” refer to in this context?]

Please look at or skim (to get the general idea – no need to print this):


There is little evidence that economic analysis of regulatory decisions has had a substantial positive impact,

Week 13. Paternalism (November 23).

Cass Sunstein and Richard Thaler, “Libertarian Paternalism Is Not an Oxymoron,” University of Chicago Law Review, 70(4)(2003), 1159–1202. Read “Introduction” (pp. 1159-1167) and skim the rest. Also downloadable in legible text at:


We propose a form of paternalism, libertarian in spirit, that should be acceptable to those who are firmly committed to freedom of choice on grounds of either autonomy or welfare.


The theory of internalities is explicitly modeled on the theory of externalities.


self-concern does not extend to other possible worlds
Week 14. Happiness Research and Economics (November 30)

**First full draft of final paper due. Papers will be returned with comments and suggestions next week.**


we argue that the happiness literature does not undermine CBA and similar conventional methods of project evaluation that rely on a money metric.


My main thesis is that economic and subjective measures – although they differ with respect to the underlying account of individual welfare – in fact are based on the very same account of social welfare: both are applications of the utilitarian social welfare function.

Week 15 (December 7). No readings for this week. We will catch up with assignments we did not have time to cover in class.

**Final Papers due – December 21.** No final exam.