CHAPTER 8. CHALLENGING THE ROLE OF UTILITARIANISM

THE ROLE OF VALUE(S) IN THE ECONOMICS DISCIPLINE

CHAPTER OBJECTIVES

In this chapter, you will learn about:

- Value Theory in Economics
- Value as it is Defined by Orthodox Economics
- The Relationship between Utilitarian Philosophy and the Economics discipline.
- Critique of the Utilitarian Approach.
- The Application in Economics of Philosophies other than Utilitarianism.

8.1 ECONOMICS AND VALUE

LEARNING OBJECTIVES

By the end of this section, you will be able to:

- Define the term value.
- Identify different interpretations of the term value.

The term **value** and the concept of **value theory** have taken on two distinct definitions in relation to economic theory. The first definition of the term value pertains to the role of normative analysis within economic theory. As discussed in chapter 1, for orthodox economic thinkers there is little room for normative thinking in the rigorous world of scientific economics. Subjective or moral judgments are discouraged in favor of utilizing a positive, value-free approach that is not a statement of anyone's value judgment or subjective feelings, but rather of what "is." By the standard orthodox textbook definition, the term "value" relates to personal biases and subjective beliefs. Also, recall from Chapter 2, the positive versus normative conflict presented by orthodox economics represents a false dichotomy. As has been discussed by non-orthodox economic theorists, subjective values tend to be present in all economic paradigms and are unavoidable.

The second definition of value that is common in economics is the one most people think of when they think of the term "value." For most people when they think of the value of something, such as a product, they are simultaneously thinking of the price of that product. Therefore, the term value and the term price tend to be used interchangeably. As a result, for many economists it is important to develop a theory of value because the theory of value provides the theorist with a sense of the origin of prices. After all, if an economist can identify the root source of value, then the same economist will also understand the root origin of prices. Since prices are incredibly important informational signals, being able to explain from where prices originate adds an important depth to economic theory.

On the surface both usages of the term "value," as described above, appear to be mutually exclusive. However, closer inspection reveals two interrelated issues. Scientists, economists included, already tend to, whether knowingly or unknowingly, assert subjective values within their theories. Values not only generate a necessary entanglement of facts and values, but they then become present throughout the very act of theorizing. In the case of economics, this means that the economic ideas that theorists present will include elements of their basic worldview or, as some would say, their philosophy.

The remainder of this chapter is laid out in such a manner as to explore the role of philosophy in economics. First, the philosophical foundation of orthodox economics, and its history, is explored. As will be shown, orthodox economics relies upon utilitarian philosophy for its value-based understanding of human action and motivation. As such, orthodox economics believes that the concept of utility holds the key to understanding the origin of prices. Additionally, utilitarianism forms the basis for the ethical perspective presented by orthodox economics. Upon closely examining the orthodox story of utility, the chapter moves on to identify important limitations that develop as a result of the use of utility. The chapter then moves on to provide alternative examples from heterodox economics, pointing out philosophical worldviews outside of utilitarianism that can form the basis of economic thought. Importantly, the alternative approaches presented do not suffer the pitfalls that are present within the orthodox, utilitarian approach.

LEARNING OBJECTIVES

By the end of this section, you will be able to:

- Identify the history of utility and its relationship to economic ideas.
- Define use-value
- Contrast Adam Smith and Jeremy Bentham with regard to their view of utility.
- Contrast cardinal and ordinal utility
- Define revealed preference theory

For those interested in the study of economics the concept of utility has a long history. Going back to the time of antiquity, great thinkers such as Aristotle made reference to the importance of the creation of use-value. From an Aristotelian standpoint use-value is the idea that human material production ought to be directed toward the creation of things that benefit human beings. Aristotle prioritized usefulness and discouraged wastefulness.

The role of the utility theory of value as a central component of the preferred ideological vision of orthodox economists of today, in some ways dates back to the time of Adam Smith. Smith, continuing the Aristotelian line of thinking, also saw significance in the concept of use-value.

Use-Value – The idea that the value of an object is based on how useful the product is to the consumer. Products have an intrinsic value to their consumers.

For Smith though, use-value represented the perceived benefit that people would derive from consumption. For Smith, consumers would be more apt to buy products that they perceived as useful as opposed to products that they believed are not useful. Still, Smith's analysis remains a long way from how utility is utilized by orthodox economists.

Although Smith does not go into much further development beyond his acknowledgement that consumers attach some kind of use-value to useful items, it is clear that Smith opens the door to the potential development of the idea that utility plays a role in determining the prices of products. Consider, if utility, or use-value, is important to consumers, then, presumably, utility must play a role in determining consumers' interest in purchasing a product. Because consumer demand is a reflection of consumer purchasing interests, consumer demand will be essential to the determination of the prices of products. It is with the evolution of economic ideas in the 19th century that the relationship between utility and prices is cemented within orthodox economic thought.

In order to understand the role of utility in contemporary orthodox economics, the place to begin is with the early 19th century philosopher and political economist Jeremy Bentham. Bentham possibly had the most prominent influence on the philosophical development of utility. Bentham's perspective is known as utilitarianism. Bentham describes utility as the cornerstone of the "Greatest Happiness Principle." In Bentham's usage, utility evolves beyond a description of usefulness into the embodiment of happiness. Utilitarianism espouses the belief that people are pleasure maximizers and pain minimizers. Therefore, any action that a person engages in must be driven by the desire either to gain happiness or to reduce pain. Taken to the field of economics, in Bentham's view, people desire products because those products bring the person happiness. Clearly, Bentham's perspective had a profound effect on orthodox economics, given the many references that this textbook has made in Chapters 2 and 6 to consumers being driven to maximize their utility.

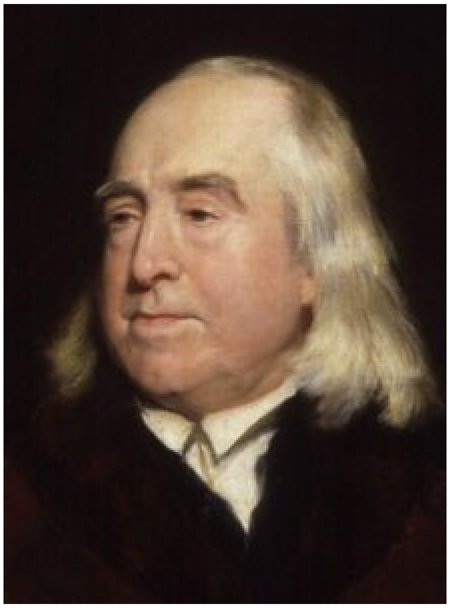
Bentham's story, for all of its applicability to contemporary orthodox economics, is still only a partial analysis. One area in which Bentham's argument is incomplete is in his treatment of the measurability of utility. When describing how a consumer may assign utility to a product, Bentham freely employed both **cardinal** and **ordinal** measures of utility.

Cardinal utility – Is the idea that the utility a consumer assigns to a product is objective and, therefore, quantifiably measurable.

Ordinal utility – Is the idea that the utility that a consumer assigns to a product is subjective, in the mind of the consumer, and is, therefore, not directly quantifiably measurable.

As a rule Bentham seemed to generally acknowledge ordinal utility as being conceptually sound in comparison to cardinal utility. Bentham understood that cardinal utility cannot be objectively measured, a person cannot be attached to a device that measures units of happy (utils). There are, however, indirect measures that can allude to cardinal utility, such as the order in which consumers purchase products. Given two products with an identical price, if a consumer purchases one of the products prior to the other, it stands to reason that the first product purchased retain greater utility than the second product. Regardless, in absolute terms, how much utility a consumer actually assigns to a product cannot be empirically measured, rendering it subjective to the consumer. Limitations aside, Bentham frequently developed examples that required cardinal measures of utility.

Another area in which Bentham's analysis was incomplete pertained to the relationship between utility and the origins of prices of products. Recall the principle of diminishing marginal utility described in Chapter 6. Bentham anticipates the idea of diminishing marginal utility by describing instances in which a person can acquire more of something but feel less satisfaction from the additional unit than they received from earlier units. Bentham's depiction, however, remains abstract rather than appearing "scientifically" concrete.



Portrait of Jeremy Bentham (Source: Wellcome Images, Wikimedia, CC-BY 4.0)

Resolving some of the incomplete features of Bentham's story are the marginalists of the 1870s. Independent of one another, a group of thinkers triggered what is now referred to as the marginalist revolution. The marginalists famously apply differential calculus to utility analysis. Differential calculus focuses on rates of change between two variables. In the case of utility, differential calculus can be used to tell a story about how, as a consumer consumes more of a product, the happiness derived from that product will change. The marginalists attempted to demonstrate, in a more concrete way, the idea that as more of something is consumed, the satisfaction or utility per unit would decline. By applying calculus, and drawing pictures to reflect the conclusions drawn from the mathematical presentation, the marginalists create the appearance of a scientific advancement in the study of utility in economics. In terms of legacy, the marginalists use of calculus is a hallmark of modern orthodox economic theory.

As much as the marginalists influence the apparatus of modern orthodox economics, their analysis still remained incomplete in that the marginalists do not resolve the issue of ordinal versus cardinal utility. It is not until the 20th century that orthodox economic theorists settle on the use of ordinal utility as the foundation of their measurement of utility. The thinker most responsible for solidifying ordinal utility's place within economics is Paul Samuelson. Paul Samuelson develops a theory known as Revealed Preference. On the surface, revealed preference theory articulates the idea that the amount of utility that any one person derives from the consumption of a product is purely subjective to the consumer in question. However, once a consumer identifies that which brings them the greater happiness, the consumer then reveals their preferences to everyone by consuming the product that they desire. In this respect, revealed preference theory seeks to quantify utility by identifying utility as a consequence of a consumer's actions.

THE APPLICATION OF UTILITARIANISM WITHIN ORTHODOX ECONOMICS AND ITS IMPLICATIONS.

Whether an unwitting or a conscious choice, utility continues to be the preferred philosophical starting point for contemporary orthodox economists. Utility also carries with it a specific interpretation of human actions and interactions. Recall, for orthodox economics, the human being is a hedonist continually in search of greater pleasure or diminished pain. Any socially determined characteristics are given (not analyzed, merely accepted), yielding an isolated utility maximizer. Also, recall, that this notion of a hedonistic person is deeply controversial with respect to its application in economics. There simply does not exist irrefutable evidence that individuals only pursue products because those products provide the individual with pleasure. Human motive can be defined in many ways with hedonism being just one of many interpretations.

Regardless of its accuracy or inaccuracy, orthodox economists perceive that, for individuals, utility is maximized through the act of exchange. At any particular point in time, an individual, possessing an initial endowment (income), begins engaging in the act of exchange with some other individual economic agent. As all exchanges are assumed to be voluntary, any exchange that two parties are willing to engage in must be an exchange that will make both parties better off, otherwise neither party would engage in the exchange. Because being made better off means, according to orthodox economic theory, acquiring more utility, the act of exchanging is the act increasing one's holdings of utility. Any and all exchanges then must be increasing individual, and subsequently, society's total utility. Presumably, once some kind of round of exchanges is complete, any and all parties that engaged in exchanges are now better off because now they have more utility as a result of their exchanges.

Of course, no one really knows whether or not the result of these exchanges really has made the participants better off or worse off because there is no device that measures utility. Utility is purely subjective and non-empirical, which means that the revealed preference argument yields an outcome in which it must be assumed that all exchange participants are made better, otherwise they would not have participated in the exchange. Assuming people are better off does not mean that people are actually better off.