CHAPTER 3

The Main Concepts

1 David Hume and the Health Fanatic

In order to be able to make full use of the simple key to the analysis of economic policy questions that I have promised to supply in Chapter 1, it is necessary to clarify a few basic concepts. Boring, perhaps, but essential, like some boring facts that one invariably has to learn in order to practise any applied science. The essence of the concepts that constitute the simple key to the analysis of policy problems, including economic policy problems, was set out about 250 years ago by the great philosopher, David Hume.

Hume pointed out that if you ask somebody

> . . . *why he desires health* he may . . . reply, that *it is necessary for the exercise of his calling.* If you ask, *why he is anxious on that head,* he will answer, *because he desires to get money.* If you demand *why? It is the instrument of pleasure,* says he. And beyond this it is an absurdity to ask for a reason. It is impossible there can be a progress *in infinitum;* and that one thing can always be a reason, why another is desired. Something must be desirable on its own account, and because of its immediate accord or agreement with human sentiment and affection. (Italics in the original)[1]

This book would be worthwhile if it did no more than drive home this message.

Hume's example illustrates in a very simple way the difference between two kinds of proposition. The first kind are 'positive propositions'. As explained in more detail later, these are propositions like 'Mount Everest is

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the highest mountain in the world' or that 'other things being equal, a rise in the relative price of apples will generally reduce the demand for them'. The truth or otherwise of such propositions can be checked – at least in principle – by reference to some facts.

The second kind of proposition is a 'value judgement', like 'happiness is *intrinsically* good' or 'killing people is *intrinsically* bad'. In the next section I shall discuss these propositions in slightly more detail. Meanwhile, it is useful to see how these two types of proposition work in David Hume's example. In Hume's story the man in question is claiming that health has '*instrumental*' value for him. His claim involves two positive propositions; namely that good health is necessary for his calling and that his calling is necessary for earning money. These positive propositions are open to reasonable challenge. For example, it could be argued – however implausibly – that he would make more money if he stopped wasting his time in the gym or swimming up and down the pool, and spent it directly trying to make money instead. But Hume's point is the one that is central to the whole thrust of this book, namely that even if we accept the sequence of positive propositions in question, in the end we have to make a value judgement, such as that happiness – or pleasure in Hume's example – has intrinsic value.

2 Value Judgements and Intrinsic Values

So what exactly is meant by the term 'value judgement'? Unfortunately, there does not seem to be any universal agreement among philosophers about what the term really means. So I shall not presume here to give an authoritative definition of the concept. Not being a philosopher I need not fear breaking any union rules if I state that I shall simply use the term 'value judgement' to indicate judgements that do not depend on factual observation or evidence in the way that, say, positive propositions depend. They cannot be shown to be either unequivocally true or false. They represent *intrinsic* values.

This definition of the concept of a 'value judgement' may appear to depart from the normal meaning of the words 'value' and 'judgement' taken separately. In ordinary life one may pass judgements about the value of all sorts of things without, in any way, implying that they have intrinsic value as distinct from instrumental value. For example, when one judges that a certain vase is valuable, one may be referring merely to its market

value and not implying that it is intrinsically valuable. But when the two words 'value' and 'judgement' are combined in the term 'value judgement' they take on a special meaning in which something or other is claimed to have *intrinsic* value.

It is true that there has been much discussion in philosophy over the years about whether all value judgements have to be justified, in the end, by some reference to facts. But although this meta-ethical topic has provided a good living for many philosophers over the ages, I shall bypass it and simply use the term 'value judgements' as defined earlier to refer to values that are held to be *intrinsically* valuable – that is, valuable for their own sake and not because they contribute to some other value.

The point is that many philosophers would agree that intrinsic values, including ethical principles, are not part of the fabric of the universe like the speed of light that can, *in principle*, be confirmed or refuted by appeal to some facts, or that can be deduced from some axioms by a process of logical reasoning. David Hume went as far as to argue, in his *Treatise on Human Nature,* that 'reason' has no place in the justification of values, or what he called the 'passions'. According to Hume reason only comes into play in the evaluation of what we now call 'positive propositions'. He argues that 'Reason is the discovery of truth or falsehood. Truth or falsehood consists of an agreement or disagreement either to the *real* relations of ideas, or to *real* existence and matter of fact . . . Moral distinctions, therefore, are not the offspring of reason. Reason is wholly inactive, and can never be the source of so active a principle as conscience, or a sense of morals'.[2] In a similar vein John Stuart Mill summed up the situation when he stated that 'Questions of ultimate ends are not amenable to direct proof'.[3]

Of course, if the question in Hume's example were put to somebody else she might not have followed the same sequence of reasons as did the man in that example. Instead, she might have gone directly to the assertion that health had intrinsic value. And that view is not open to reasoned challenge, even though some people might regard it as being a bit bizarre. It would be a value judgement, so that is the end of the story. But the point that Hume was making was that even if we accept the chain of positive propositions attributed to the man in his example, in the end he still has to justify his policy by reference to some intrinsic value, which, in his case, is his pleasure.

And it is possible that another person to whom Hume's question is put might have replied that he regarded health as having both intrinsic value – a value judgement – and the *instrumental* value of leading to happiness via the money-making route set out. In the former case it is the end of the story. In the latter case the positive propositions involved may be subject to challenge, but even if they are accepted, it is still necessary to justify the pursuit of health by some value judgement, such as that happiness is intrinsically valuable. There cannot be any generally accepted list of top-level intrinsic values. For example, at the level of the individual, they might comprise Aristotle's list of basic values, including virtue, honour, pleasure and understanding.[4] Still at the level of what are intrinsic values for an individual, some contemporary philosophers have listed 'certain states of consciousness; personal relationships; intellectual, artistic, and moral excellence; knowledge; and human life itself'.[5]

But some valuable features of society as a whole are about relations between the constituent individuals, and are not simply aggregates or averages of individual values. This would be the case, for example, with justice or social harmony. These are characteristics of society as a whole, not of individuals. Indeed, on the first page of his famous book, *A Theory of Justice*, John Rawls wrote that 'Justice is the first virtue of social institutions, as truth is of systems of thought'.[6]

Aesthetic judgements are also a form of value judgement since they are not amenable to empirical verification. For example, no appeal to facts can help decide whether some pieces of music are 'better' than others. Some people may claim that this is not true and that, for example, some music is 'better' than other music on account of certain 'facts', such as its harmonic subtlety, popularity or richness of emotional response. But while some of the facts may be indisputable the choice of criteria is a value judgement. Suppose a piece of music is judged better on one of these criteria but worse on another. What factual evidence could prove which criterion is more important? And how is it that some music that had been poorly regarded in the past is now very popular, or vice versa? Had some new factual evidence come to light, or did tastes or values simply change?

How does the previous distinction between positive propositions and value judgements operate in welfare economics? To answer this question we need to say a little more about 'positive propositions' and to introduce also the concept of a 'normative proposition'.

3 Normative Propositions and Positive Propositions

A 'normative proposition' is an 'ought' proposition – that is, an assertion about what *ought* to be done, like 'you *ought* to be kind to animals' or 'you *ought* to respect your teachers' or 'we *ought* to raise taxes on fattening food'. Such propositions differ sharply from 'is' propositions – that is, 'positive propositions' – such as those explained in Chapter 3, namely that Mount Everest is the highest mountain in the world, or that, other things remaining equal, the demand for apples is inversely related to their price. The distinction between normative and positive propositions corresponds to the famous distinction drawn by David Hume between 'ought' propositions and 'is' propositions. Hume was highly critical of a widespread tendency to jump too readily from the latter to the former.[7] Unfortunately, his criticisms were not enough to banish this tendency and it is still widespread. In fact, the main object of this book could be seen as an attempt to fight against its widespread persistence in the analysis of economic policy.

As indicated earlier, since *positive propositions* are factual statements about the way the world *is*, including statements about how it is believed to work, it must be possible – at least in principle – to check their truth by reference to some facts. They may be simple descriptive propositions, such as that the population of the USA is greater than that of Canada. Or they may describe certain causal relationships that are believed to hold between certain economic variables, such as the relationship between inequality and economic growth.

Of course, value judgements will influence the choice of 'facts', or the particular economic relationships, that are examined. This is why there can never be a value-free *positive economics*. For the choice of problems to be studied – such as the causes of inflation, or the effect of growth on the environment, or the degree of inequality in society and so on – depend on value judgements. Value judgements will also enter into the definition of the variables included in any analysis. For example, in an analysis of, say, the degree of economic inequality in society, there are different ways of measuring inequality. These include inequality of incomes between individuals, families, households, post-tax income or pre-tax income, lifetime income or annual income and so on. But when one has selected a particular definition in the light – partly or fully – of one's value judgement as to which definition is more 'important', the subsequent relationship between whatever concepts of

inequality one has selected and, say, the rate of economic growth, is a matter of positive propositions. But given the particular definitions and methods adopted the statistical relationship between the selected variables *as defined* is a matter of fact and is the basis of a positive proposition. For example, this could take the form of the proposition that greater equality – as defined – does not conflict with economic growth – as defined. In other words, the truth or otherwise positive propositions can be verified, in principle, by reference to the 'facts' *as they have been defined*. So, positive propositions are value-free, although positive *economics* cannot be value-free, since the choice of problems to be studied and the way that the variables are defined depend partly on subjective value judgements.

Of course, the empirical verification of positive propositions in economics is not a simple matter. Economists cannot carry out controlled experiments as in the natural sciences or cut up corpses in order to improve their understanding of how they function. Their substitutes for these are comparisons across space – for example, between countries or regions or individuals – or comparisons over time. But in all cases the interpretation of the comparisons is invariably complicated by differences in other important variables.

Indeed, many important positive propositions in economics are still the subject of serious – and often heated – debate. These include propositions such as those about the effect of taxes on people's willingness to work, or the effect of the interest rate on the level of investment, or the effect of a budget deficit on an economy's rate of growth, etc. Propositions of this type have been the subject of an immense amount of very skilful and ingenious empirical testing, without, in many cases, arriving at indisputable results. What all such propositions have in common is that, *in principle*, given the definition of the variables involved, their truth or falsity can be established by appeal to some facts.

In practice, most informed debate about any particular economic policy or project revolves around differences in predictions about its likely effects. People – such as some politicians, or journalists, or commentators – who claim to know what these effects will be without having some model in mind of which positive propositions are relevant and what evidence for them exists are deluding themselves. But, even where there is agreement over the relevant positive propositions, the *desirability* of the policy or project in question will still depend on ultimate objectives. And these will depend on '*value judgements*'.

Before moving on, however, mention ought also to be made of one class of proposition that can be shown, in principle, to be true or false, without recourse to empirical verification. These are purely logical propositions such as those of mathematics, which, given some axioms, depend solely on the laws of logic. But such propositions are not relevant to the subject matter of this book. What is of interest here is the distinction between positive propositions and value judgements, since this is at the heart of the simple key to the analysis of economic policy issues which this book is designed to provide.

So, having set out the basic concepts needed for a fruitful analysis of any policy problems, how do they arise in the particular area with which we are concerned here, namely welfare economics? To answer this question it is useful to explain first what welfare economics is all about.

4 What Is Welfare Economics?

Welfare economics is that part of economic theory that is concerned with how far the economy is operating 'efficiently'. But the concept of 'efficiency' is meaningless except in relation to objectives. An axe may be an efficient instrument for chopping up wood, but not for trimming one's toe-nails. So what is the objective to which economic efficiency is directed? It is to make the maximum possible contribution – given available resources, techniques and people's preferences – to society's economic welfare. But 'society's economic welfare' is obviously a very subjective concept about which reasonable people may differ. For example, what do we mean by 'welfare' in general, or 'economic welfare' in particular, and what 'society' we are concerned with? And how can one assess the total welfare of a society without taking account of the way it is distributed among its members?

Furthermore, in most economic policy issues there is often no clear distinction between the objectives – that is, the 'ends' – to which one is aiming and the 'means' that may be employed to pursue those ends. For example, the ability to participate in the political life of one's community is both an 'end' in itself as well as a 'means' to influence its policies. At a more prosaic level if the authorities decided to reduce the country's dependence on imported fuel it is unlikely that they would do so by forcing aged pensioners to go down the coal mines, on the grounds that they have a low opportunity cost, since this particular 'means' to the adopted 'end' would probably conflict with most people's values, such as

the rights of old people to freedom and a quiet life. The well-known definition of economics as 'the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses' does not prescribe what the 'ends' ought to be.[8]

Thus whether an economy is operating in a manner best adapted to the promotion of society's economic welfare depends on 'value judgements', which are often – but not always – of an ethical nature, about both ultimate objectives and the means employed to pursue them.[9] As Amartya Sen has put it, an '. . . . ethics-related view of societal achievement cannot stop the evaluation short at some arbitrary point like satisfying 'efficiency'.[10] Nevertheless, given some value judgements that define our objectives, it is, of course, impossible to proceed to judgement as to how far these objectives are being achieved and, if not, what ought to be done about it, without some facts, which are in the domain of what is known as 'positive economics'

'Welfare economics' is sometimes distinguished from 'normative economics'. This distinction is significant only if 'welfare economics' is defined narrowly as being limited to the basic theory of what is known as the 'optimum' allocation of resources and the types of market failure – such as externalities, imperfect competition and so on – that prevent resources from being allocated optimally. Defined in this manner, welfare economics does not necessarily prescribe what ought to be done to improve the working of the market or to achieve other objectives that may even conflict with an 'optimum' allocation of resources.

'Normative economics', however, is usually interpreted more broadly. It encompasses considerations that lie outside the domain of pure economic theory, and which usually fall within the wider domain of ethics. It allows for the pursuit of values that may even conflict with a narrow concept of society's purely economic interests. In fact, the founding fathers of the subject – notably Pigou, Bergson, Samuelson, Little and Graaff – actually used the term 'welfare economics' in the broader sense. So out of respect for them I shall use it to correspond to the broader definition and to go beyond the basic theory of resource allocation and productive 'efficiency'. So I shall use the terms 'welfare economics' and 'normative economics' interchangeably.

For present purposes a more important – and generally adopted – distinction is one that I do follow in this book. It is the one described by one distinguished contributor to welfare economics, Tibor Scitovsky, in the following terms 'Modern economic theory draws a sharp distinction

between *positive economics*, which explains the working of the economic system, and welfare economics, which prescribes policy'.[11]

Positive economics is that part of economics that purports to explain *how* markets work; what determines how much people want to buy or sell, and how their willingness to do either depends on their incomes, prices, expectations, tastes and a host of other influences. Thus it comprises propositions such as that, other things being equal, a fall in a country's exchange rate will lead to a rise in the demand for its exports.

By contrast, welfare economics is *prescriptive,* it provides the basis for normative propositions about what *ought* to be the case. It would include, for example, the proposition that incomes ought to be taxed, or that policies ought to be implemented to deal with environmental externalities. Normative propositions are thus at the cutting edge of welfare economics, and they rest on a combination of positive propositions and value judgements.

Certain features of society may possess *instrumental* value such as, for example, an educated population or an impartial legal system. They may be instrumentally valuable on account of the contribution they are believed to make to some other value, like freedom or justice. They are often referred to as *'derived'* values. But the proposition that they are *instrumentally* valuable must be a positive proposition so that, in principle, its truth or falsity can be checked by appeal to some facts. Indeed there is considerable statistical evidence of a positive relationship between the average educational level of a society and the average self-reported happiness of its citizens. Of course, education may also possess intrinsic value. Most people probably share Aristotle's view that, for an individual, knowledge possesses both *intrinsic* and *instrumental* value.

In the end, in welfare economics, it is the normative propositions that are the object of the whole exercise. On the basis of positive propositions and value judgements one can arrive at normative propositions. And, conversely, normative propositions have to be justified in terms of value judgements and, where relevant, positive propositions. Value judgements do not have to be ethical judgements. For example, you may believe that health is intrinsically good but would not claim that somebody who did not try to stay healthy was evil. Nor would one maintain that somebody who does not believe that education is intrinsically valuable is in some way immoral.

Thus all normative propositions are prescriptive, or 'ought', propositions. They all have to be justified, *in the end*, by some form of '*value*

judgement', such as that being richer or having beautiful flowers is *intrinsically* good, or that killing people is *intrinsically* bad. As such they are not open to empirical verification. This does not mean that there is no room for discussion as to the consistency of some particular values with others, as in the aforementioned example of the value judgement that 'killing people is bad'. Similarly, somebody who is against abortion on the grounds that human life is 'sacred' might want to ask himself whether this is consistent with his views on the morality of capital punishment, or some other social value, and if there is a conflict of values how he would trade them off. In such cases one comes up against the possible conflict between intrinsic values, which are discussed in more detail in Chapter 10 in connection with the ethical doctrine known as 'Utilitarianism'.

5 The Construction of Welfare/Normative Economics

In welfare economics value judgements are subjective judgements about what values society should adopt for the purposes of defining its economic objectives and the means that should be used to promote them. They are not *necessarily* ethical judgements in the usual sense of the term 'ethical'. But in economic policy debate the value judgements usually do involve ethics, if only implicitly. For, in principle, economic policy choices should be based on (i) models of how economies, or parts of it, are believed to operate; and (ii) the relevant objectives that society ought to pursue and the acceptability of possible means to pursue the objectives. The first part of this system comprises the 'positive economics', which relies on what one believes to be 'facts'; and the second part relies on some value judgements, which may be noble or obvious, but which are not subjects for empirical verification.

The recipe for normative propositions in economics could be set out as shown in Fig. 3.1. First, make some '*behavioural*' (psychological) assumptions about how economic 'agents' – consumers and producers – react to the economic environment with which they are faced. This would include their assets, relative prices, demand for their services and so on. These behavioural assumptions could include, for example, the assumption that rational agents attempt to select, from the options open to them, the ones they prefer. Then mix these behavioural assumptions with some assumptions about technology – such as the law of diminishing marginal product. With this mixture one can

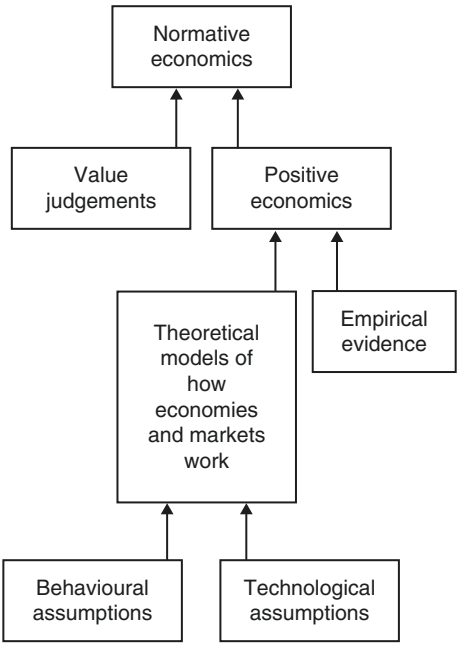

Fig. 3.1 Structure of economic policy choice

construct a nice *theoretical* model of the way that markets would function. If one can then stir in some factual evidence to demonstrate how far the theoretical assumptions of the model are valid one arrives at some *positive economics*.

Most empirical work in positive economics is devoted precisely to the verification of these assumptions. And even some highly plausible behavioural assumptions have been challenged. For example, many studies by behavioural psychologists have shown that consumers' behaviour is not as 'rational' as is generally assumed in the models (Chapter 5). Indeed, it has been claimed that the rational choice model that is at the heart of positive micro-economic theory is not a 'positive' theory to start with and is really a 'normative' theory of how people *ought* to behave.[12] On the other hand, many statistical studies do confirm that, in the end, some of the basic predictions of the theory hold good. Demand curves do tend to slope down from left to right – on the whole – and where they do not there is usually a convincing theoretical explanation.

But, as we have seen, even when the economist has established a plausible, workable model of how the economy – or that part of it in which one is interested – is believed to work, it is still impossible to make normative policy prescriptions without, at some stage, introducing some value judgements.

For David Hume there was only one basic value for an individual that was desirable for its own sake, namely 'pleasure' or 'happiness'. In later years, in the hands of Jeremy Bentham and others this was identified with 'utility'. Furthermore the 'utility' of society was simply the sum total of the utility of the individuals comprised in that society. This school of thought – namely that there was one top-level value, utility – became known as 'Utilitarianism', a school of thought that still commands very widespread assent. It is discussed in more detail in Chapters 9 and 10.

It is also widely contested. Many philosophers believe that there are several independent intrinsic values and that they are incommensurate. In fact most of us subscribe to several values which often appear to conflict. For example, one might be faced with an occasional conflict between truth and loyalty to some other individual or institution. And, at the level of society as a whole, it may be believed that the intrinsic value, justice, conflicts with other intrinsic values, such as freedom or the role of prosperity in raising happiness by one means or another.

But whether one is a Utilitarian, or a pluralist who believes that there are several top-level values, it is still true that, faced with any normative proposition, one cannot go on for ever asking for the reason behind the reason for it without reaching the point where reason has no more role to play and one has reached an *intrinsic* value judgement, like 'pleasure' in Hume's example at the beginning of this chapter.

As indicated earlier, most research and public debates about economic policies tend to ignore – quite reasonably – the value judgements involved and concentrate on disagreements about the consequences of different policies. This book is intended to remind readers that the value judgements are there, and are an essential part of welfare economics and that their neglect can often lead to an easy acceptance of certain policies that depend on some possibly contentious value judgements. Without some idea of what *ends* we want to attain there is little point in knowing what economic *means* will attain them most 'efficiently'. It would be like studying anatomy or physiology without expecting it to be of any practical use. A value-free welfare economics would be rather frustrating.

Notes

1. Hume, 1739, 1998 edn., ed. Beauchamp: Appendix 1, para. 19.
2. Hume, 1739, www.davidhume.org:3.1.11.10. Hume's defence of his theory of morality in general and of justice in particular was also presented, more briefly, just over ten years later, in *An Enquiry concerning the Principles of Morals.*
3. Mill, 1861:I,5.
4. *Ethics, 1097b2–21.* Aristotle did not, however, regard these as what he called 'final values', of which, in his opinion, there was only one, namely 'happiness' (interpreted in a rather special manner). The reason he gives for this is that although we might pursue them for their own sake, one might also pursue them for the sake of our happiness, whereas the converse does not apply.
5. Scanlon, 1998:87.
6. Clarendon Press, Oxford, 1972.
7. Hume, 1739, *ibid*:3.1.1.27.
8. This definition originated in the important and influential book by Lionel Robbins, 1932. It abstracted from the question of how far an economy's 'scarce means' are fully employed, since it was focused on the problem of allocation under conditions of scarcity.
9. See an interesting discussion of this point in Jonathan B. Wight, *op.cit.* 59 *et seq.*
10. Sen, 1987:4.
11. Scitovsky, 1941:77.
12. See Hands, 2009:13.