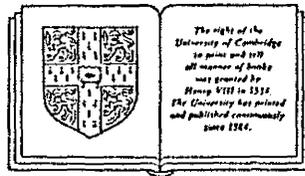


RAFFAELE MATTIOLI FOUNDATION

Alan Peacock

*PUBLIC CHOICE ANALYSIS
IN
HISTORICAL PERSPECTIVE*



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1. Introduction

Political Economy or Public Choice is an important area in which great progress has been achieved and important insights have been gained. It is not part of conventional economics but is by most economists seen as an aspect which may be taken into account if one likes – but which one can disregard without any problem at all. I therefore greatly welcome Professor Peacock's Mattioli Lectures, and I would like to congratulate the organizers on having chosen Sir Alan, one of the most influential and prolific researchers in political economy.

It goes without saying that I greatly enjoyed the Mattioli Lectures. I personally am convinced that the views proffered by Professor Peacock cannot be overestimated, views which are based on a broad perspective of the issues, a concentration on relevant problems, combined with a clear reasoning. This approach compares favourably with much of current economics, and I am sorry to say, also part of Public Choice, which tends to be reduced to some kind of applied mathematics.

I should like to concentrate my remarks on two aspects: the message of Political Economy, and the role and use of the History of Economic Thought.

2. The Message of Political Economy

a. Political fails: In Political Economy (a term which I prefer to the rather narrow concept of "Public Choice") it is generally accepted that political processes do not function perfectly. Rather, all decision-making mechanisms "fail", i.e. they have shortcomings which prevent them from functioning optimally or even efficiently. It has been shown by Political Economists that democratic procedures do not necessarily lead to social welfare maximization (however defined) but that they may

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lead to contradictory and irrational results. The failure of decision making by bureaucracies and by bargaining among interest groups has also been the subject of analysis, and has been stressed in Professor Peacock's lectures.

The study of the "failure of politics" undertaken in Political Economy has been a reaction to "market failure" as proposed by welfare economics in the 1960s. At that time (and some economists still believe in that view) it was generally accepted that when market failure exists, government intervention is automatically needed. For political economists it is, in contrast, clear that this conclusion is unwarranted, and that a comparative evaluation of the workings of the various decision-making systems is needed.

In much of (American) Public Choice a further conclusion has been reached: it is argued that markets are generally superior, and that politics is almost always inferior. However, this conclusion is based more on an ideological presupposition than on analysis, and it certainly does not follow from Political Economy.

b. The real message: In Sir Alan's lectures the value of democracy in comparison with an authoritarian system has been treated more implicitly than explicitly. Democracy can, and should, be looked at as that decision-making procedure taking individual preferences into account, or enabling the orderly change between parties in power according to election results. Analysing these aspects in depth, Political Economy has provided new and relevant insights which compare most favourably with the naive view of orthodox economics which assumes either that no government exists, or that governments automatically maximize social welfare quite irrespective of their form. It is indeed assumed that the government behaves in the same way whether it is a dictatorship or a democracy.

What matters is not the juxtaposition of market failure with political failure but to compare democratic with authoritarian decisions. In his lectures, Sir Alan refers to Lord Keynes' "Harvey Road mentality", the view that the cognoscenti or the intellectual aristocracy should and must tell people what has to be done. This view corresponds at best to a benevolent

dictatorship, but in most cases turns out to be far from benevolent. The real message of Political Economy thus has to do with the virtues of democracy compared to other political decision-making systems.

c. The dangers of authoritarianism: It could be argued that the emphasis on the virtues of democracy here postulated are of little relevance because we fortunately live in democracies, and authoritarianism is no real danger. However, I would like to submit that there is always the danger of lapsing into this direction. Indeed, it may often be observed in our democracies that solutions to social problems are sought by resorting to dictatorial measures, disregarding democratic procedures and individual preferences.

An example is the modern ecological movement which is of considerable importance today in Germany and Scandinavia, and which has recently gained momentum in France, and is predictably important also in Italy. Many of the "Greens" have a marked tendency to deal with environmental problems by applying draconian measures. Environmental policy is solely seen in terms of prohibitions, and those damaging nature must be harshly punished. Those not agreeing with this policy tend to be considered criminals, to be treated as outcasts losing their human and political rights.

Political Economy shows convincingly that this approach implies two major mistakes. The first is that a disregard for preferences of some parts of the population leads to a resistance to the well-meant policies undertaken. As a result, the policies have only partial effect. The second mistake is that a reliance on prohibitions necessarily requires the intensive use of public bureaucracy. Public officials, however, pursue their own ends, thus diverting from the intended goals.

3. The Role and Use of the History of Economic Thought

a. Its usefulness: Sir Alan has persuasively argued that the history of economic doctrines is of great use for understanding political economy, and the economy in general. (But he also

pointed out that there are opportunity costs involved.) He concludes that a knowledge of our past economic masters' thinking is a necessary but not a sufficient condition for good economics.

b. Is it in fact useful? I would like to take a somewhat different view. The problem is not that there are no important ideas with former economists, rather the contrary is true: there are few ideas which could not in some form or other be detected in the writings of the classics.

The problem is that these ideas cannot be seen, or grasped, in the writings of the dead masters, without having the idea *before-hand*. What happens in effect is that the ideas and theories are looked up in the past writings only after such ideas have been discussed in modern analysis. It is often an *ex post* exercise, a kind of make-up, which not rarely serves solely the purpose of exhibiting one's erudition.

To support the proposition that the history of economic thought is mainly of *ex post* use, three areas may be mentioned:

(i) *Social accounting*: As is well known, this analysis was developed by Richard Stone and James Meade in Britain in order to better evaluate the resource constraints of the Second World War effort. Only later was it discovered that at the end of the seventeenth century Gregory King was engaged in the same endeavour, including a prediction of how long it is possible to pursue a particular war.

(ii) *Preference aggregation*: In the early 1950s Kenneth Arrow proved that no aggregation of individual preferences meeting reasonable and democratic conditions is generally possible without risking logical inconsistency.¹ This study has had great impact on economics, and has brought to light a new area of enquiry, social choice. It became known only later, mainly through the works of Duncan Black,² that there are many precursors to Arrow's

1. KENNETH J. ARROW, *Social Choice and Individual Values*, New Haven: Yale University Press, 1951 (Second edition, 1963).

2. DUNCAN BLACK, *The Theory of Committees and Elections*, Cambridge: Cambridge University Press, 1971.

findings. Indeed, scholars like Lewis Carroll (the Reverend Dodgson, student of Christ Church, Oxford, and author of *Alice in Wonderland*) have extensively written about the preference aggregation paradox, and have even applied it to practical problems.

(iii) *Party competition*: One of the most influential books in Modern Political Economy has been Anthony Downs' *Economic Theory of Democracy*, published in 1957.¹ No reference was made by him, nor by the writers following him, to Joseph Schumpeter who in his *Capitalism, Socialism and Democracy*, published in 1942,² very clearly discussed party competition. Indeed, in many respects, Schumpeter went further than Downs. Nevertheless, nobody engaged in the early efforts to develop party competition theory in early Public Choice remembered this important forerunner. This is all the more surprising because Schumpeter was in his time, and is still today, one of the most famous economists.

How can this incapacity to take up the relevant ideas in the works of the past masters at the right time be explained? I should like to suggest that there may be two quite different kinds of knowledge contained in the writings of the past. The first type of knowledge is perceived, and there is no problem to retrieve it. The second type of knowledge cannot be put to use because it is outside one's consideration or outside one's *ipsative possibility set*.³

4. Consequences

What are the conclusions to be drawn for the teaching of the history of doctrines to students of economics? Based on what has been said above, two possibilities suggest themselves:

1. ANTHONY DOWNS, *An Economic Theory of Democracy*, New York: Harper and Row, 1957.

2. JOSEPH A. SCHUMPETER, *Capitalism, Socialism and Democracy*, New York: Harper, 1942.

3. See, for a discussion of this concept, BRUNO S. FREY, 'Ipsative and Objective Limits to Human Behaviour', *Journal of Behavioral Economics*, Winter 1988, pp. 229-48.

(i) Students could be taught to actively exploit the ideas contained in the writings of the past masters. This solution is not attractive because it means that history is used instrumentally, only. More importantly, it does not appear to be feasible after what has been said above: if one does not have an idea beforehand, one does not know what to look for in the past literature.

(ii) The second solution is to leave the situation as it is today, i.e. not to expose students – and in particular beginners – to any special training in the history of economic thought. This solution is based on the notion that the history of economic ideas is such a fascinating and beautiful topic that only those people should study it who do it voluntarily and on their own initiative; but no student should be *forced* to engage in it. It is too valuable a subject to be imposed upon people who might resent it (partly due to the opportunity costs mentioned). Rather, the history of economic doctrines should be reserved for accomplished and cultured scholars who do not only love it but also put it to good use. In his Mattioli Lectures Sir Alan has given us a delightful example of such an undertaking.

