

PART I

Defining Economics, Methodology, and Models

CHAPTER 2

DEFINING ECONOMICS, METHODOLOGY, AND MODELS

Defining Economics

To define economics, it is necessary to differentiate between what is the subject matter and what is the research strategy (that is how to explain the subject matter) and the various research methods used to carry out the explanation. However, there is one problem in that what constitutes the definition of economics is, as is the case for mainstream economics, collapsed into a particular research strategy and research methods, such as modeling and econometrics. And this strategy and methods are then argue to constitute or defines economics. Consequently, alternative strategies and methods are deemed to not be economics or relevant to economics. But it is necessary to differentiate what constitutes the subject matter of economics and the research strategy and methods used to examine it.

The basic subject matter of economics consists of the flow of goods and services required by society to meet the reoccurring needs and promote the well-being of those who participate in its activities. That is, people have social lives; they have families, parents, children, and a history; and they need to be feed, housed, clothed, married, and schooled. And the needed and desired goods and services are produced to sustain their socially constructed, meaningful lifestyle—this is called the *provision process*. Thus the provisioning process must be a continuous, non-accidental series of economic activities taking place through time that provide individuals and families the goods and services necessary to carry out their individual and social activities. Hence economic activities are linked to and embedded in various stable societal institutions

(such as the legal system, family, and the state); in cultural values (such as individualism and egalitarianism) that are evaluative criteria for establishing which social activities are worthwhile and desirable; and in norms and beliefs (such as property rights and the work ethic) that explain or justify particular social activities. These components or structures of the social fabric affect the pattern and organization of economic activities underpinning the provisioning process. So the defining task of economics is explaining the process of provisioning. This task is often articulated in mainstream introductory textbooks as ‘what will be produced?’ ‘how will it be produced?’, and ‘who will get what is produced?’; but it amounts to the same thing. Finally, it should be noted that since the time of Sir William Petty or Adam Smith to the present day, the subject matter of economics and economics defining task has remained the same, or less.

What has changed, however, is how the provisioning process or the ‘what-how-who’ is explained. While the generic explanation is a secular or materialist explanation (relative to a religious explanation for example), there are in fact two distinct explanations of the provisioning process: heterodox and neoclassical/mainstream. The heterodox explanation focus on human agency in a cultural context and social process in historical time affecting resources, consumption patterns, production and reproduction, and the meaning (or ideology) of economic activities engaged in social provisioning utilizing empirically grounded concepts and an open system, grounded theory methodology—thus its explanation conceives the provisioning process as a *social provisioning process*. The neoclassical explanation focus on how asocial, ahistorical individuals choose among scarce resources to meet competing ends given unlimited

wants—thus its explanation conceives the provisioning process as an *asocial provisioning process*.

Methodology: Research Strategy and Research Methods

Research strategy is about conceiving how to go about creating explanations of the provisioning process and evaluating those explanations. Within mainstream economics, its research strategy has evolved over time, mostly from a less to a more cohesive strategy in which assumption and axiomatic-deductive arguments generate theories (that is explanations) that are articulated with mathematics and presented and engaged with through models; and they are evaluated through the use of correlative statistics, such as those generated by regression analysis. What is important here is that the theories are secular explanations of a real provisioning process located in a real world—that is a world that exists independent of the individual. But a particular assumption is made about this world of the provisioning process in that the economic events that are being theorized about are not causally related but rather are correlated; and along with this is the view that theorizing about the provisioning process is separate from and hence not grounded in the actual provisioning process. This is clearly seen in terms of the distinction between theory-model and evaluation—but more on this below. To see how the mainstream research strategy and research methods evolved over the 20th century, let us start with Alfred Marshall.

Alfred Marshall

In the period 1890 to 1920, economics was typically defined as the study of the causes of the material welfare that affect the wellbeing of individuals and society.¹ This definition was not significantly different from the definition of political economy in the first part of the 19th century. What is significant about it is that economics is defined in terms of content, in terms of subject matter. Given the above, it is unremarkable that Marshall conceived of economics as

...a study of mankind in the ordinary business of life; it examines that part of individual and social action which is most closely connected with the attainment and with the use of the material requisites of wellbeing. Thus [economics] is on the one side a study of wealth; and on the other and more important side, a part study of man. [Marshall 1972: 1]

But there is much to be noted in this definition. First, the *individual* in the definition is conceived as self-reliant, independent, and makes decisions about choices with deliberation and forethought—a forerunner to the rationality assumption concerning economic actors. Moreover, Marshall assumed that the individual’s motivation for economic activity, that is his/her efforts (or work) to satisfy wants (utility), is the pay or money s/he gets for their efforts. So, money is the measure of motives with regard to the economy. However, because different individuals can evaluate the same amount of money of income differently and get different benefits (that is they have different marginal utility of money), it is difficult to generalize across them. Marshall gets around this problem by placing the individual in a group and then taking the “average”. Thus,

¹ See for example, Wicksell (1977: 2, first published in 1901), ...; also see Robbins (1969), Howson (2004), and Backhouse and Medema (2009a).

Marshall's entire analysis of economic activities through the use demand, supply, prices, and distribution is done in terms of the "representative" consumer and firm.

Secondly, considering the concept of *wealth*, Marshall defined it as all things that satisfy human wants directly or indirectly and denoted them as *goods*. Some utility generating goods, such as free goods or personal non-transferable goods are not or cannot be demanded by others, do not fall within the domain of economics. Marshall defined *economic goods* (that is goods that fall into the domain of economics) as:

...all those things, external to man, which (i) belongs to him, and do not belong equally to his neighbors, and therefore are distinctly his; and which (ii) are directly capable of a money measure,--a measure that represents on the one side the efforts and sacrifices by which they have been called into existence, and, on the other, the wants which they satisfy. [Marshall 1972: 47]

In defining economic goods in this manner, Marshall did the following. First he introduced the notion of *scarcity* defined in terms of relative demand; and at the same time he also introduced the notion of private property. Thus an economic good is one that is scarce and one that exists within a legal system of capitalist private property. Secondly, an economic good has value for exchange and most significantly requires that exchange takes place. That is, economic goods and their exchange arises because of their utility to others, private property, and scarcity.² Finally, he has the economic good being measured in terms of money/prices; and this same good represents the utility of the consumer and the efforts and sacrifices that went into producing it. Hence since money

² This tripartite foundation of exchange is found among all neoclassical economists. Wicksell (1977: 18) makes this quite clear. Consequently, if utility and/or scarcity did

measures utility and efforts and these in turn are driven by economic motives, such as maximization, money thus prices are indirect measures of these motives.

Economic goods can be divided into two kinds, *material goods* which are subject to rights of private property and thus can be transferable and exchangeable and which include produced and non-produced material things such as land, houses, machinery, and financial notes, and *non-material goods* which can be acquired and are used to obtain material goods and which includes business or professional practice, especially “goodwill”, which can be transferred by sale to a newcomer. In defining wealth and economic goods as he did, Marshall was forced to characterize economics as a one-way-street of the production of utilities. That is, since wealth consists of goods that satisfy wants and economic goods as those species of goods that are used directly or indirectly to satisfy wants, economics simply becomes the study of a one-way-street that consists of the use of non-produced economic goods combined with produced economic goods and non-material economic goods to produce utilities, that is economic goods that satisfy wants.

Finally, the definition of economics excludes any mention of politics: “it shuns many political issues, which the practical man cannot ignore: it is therefore a science, pure and applied, rather than a science and an art” [Marshall 1972: 36]. By pure science, Marshall means economic theory while applied science refers to the application of theory to the various fields of economic activity. In distinguishing between science and art he was rejecting the view associated with the term political economy that understanding how the economy works can not be separated from politics and ideology. This enabled

not exist as meaningful, coherent concepts, then exchange (as conceived in neoclassical

Marshall to argue that economics was a science and economists were authoritative experts on how the economy worked: for they asked and answered such questions as ‘what are the causes which affect the organization of industry and trade?’ and ‘what increase of wellbeing is *prima facie* likely to result from a given increase in the wealth of any class of society?’. Hence they could provide expert advice to the politicians.

Research Methodology

The aim of economics is to develop economic laws, which for Marshall were no more than a general proposition or statement of tendencies that were based on economic motives that were measured by money. The laws themselves were based on *normal* conditions—that is the systematic forces which operate in the long period: “normal economic action is that which may be expected in the long run under certain conditions (provided those conditions are persistent)....” [Marshall, 1972, p. 28]. Moreover, for normal conditions to hold and the systematic forces work themselves out, *all other things must be held constant*. The introduction of the *ceteris paribus* assumption was necessary, Marshall argued, to do any theorizing and arriving at economic laws. The assumption eventually becomes a core methodological feature of modern neoclassical microeconomics. Marshall identified the concern with economic laws as *pure economics*,

for, in order that a proposition may be of broad application it must necessarily contain few details: it cannot adapt itself to particular cases; and it points to any prediction, that must be governed by a strong conditioning clause in which a very

theory) will not exist. This point shall be returned to later in the monograph.

large meaning is given to the phrase “other things being equal.” [Marshall 1972: 31]

To construct economic laws, that is to do economic theorizing or pure economics, Marshall argued that both induction and deduction were needed as well as the free play of the imagination. In particular he stated that

Induction, aided by analysis and deduction, brings together appropriate classes of facts, arranges them, analyses them and infers from them general statements or laws. Then for a while deduction plays the chief *role*: it brings some of these generalizations into association with one another, works from them tentatively to new and broader generalizations or laws and then calls on induction again to do the main share of the work in collecting, shifting and arranging these facts so as to test and “verify” the new law. It is obvious that there is no room in economics for long trains of deductive reasoning.... [Marshall 1972: 644]

While imprecise it does give the tenor of how Marshall set about developing his theories. All his assumptions and arguments in *Principles* are of this form, in particular he tries to ensure that there are facts underlying them.³ However, Marshall (along with all other neoclassical economists) did not apply this approach to developing particular theoretical concepts, such as utility, scarcity, or marginal products.

Research Methods-Models and Mathematics

The complex interdependencies of the real world are made manageable by partial equilibrium analysis.⁴ The dynamic elements are removed by specifying some essential characters. In Marshall’s theory these characters are wants, agents of production, and

³ Wicksell (1977: 9) made a similar argument.

technology. Once these are fixed, the world is fixed. After setting these basics the economist is still confronted with an infinite number, in time and space, of interdependent variables. The most “important” of the causal relationships are then chosen for study. The rest of the relationships are held constant, and importantly, so are any interactive effects of one variable on another. With this apparatus, one conducts the comparative static experiment, that is, moving one variable to see the immediate effect on another, *ceteris paribus*. But here is a problem: if the initial variable moved, how can all else remain constant? One variable cannot change without corresponding changes in other variables. Other variables must change to allow for the change of that one. For example, how can one posit change in price of one good without a corresponding change in something else in the economy related to it? The supposition that leads to the escape from the quandary is that all such offsetting changes are assumed to occur in one of these three ways: 1) the changes occur in a sector of the economy irrelevant to the one scrutinized; 2) the change is simply not substantial enough to matter; 3) or the change occurs uniformly over all economic participants. Thus, any offsetting change has no or very little effect on the partial static analysis.

⁴ Reference to Maki.

CHAPTER 3

MODERN ECONOMICS, METHODOLOGY, AND MODELS

- I. Defining Economics
- II. Methodology of Neoclassical Economics
 - A. Observation and measurement – real world; content of the real world is accepted
– real world exists
 - B. Constructing Explanation to Model Building
 - 1. Concepts and components for modeling building: non-empirically grounded-fictitious; deductive argumentation; role of assumptions
 - 2. Role of mathematics
 - C. Testing Models – evaluating the model: econometrics—comparing the outcome of the model to data
 - D. Models as knowledge

Robbins: definition, eliminate content; value free, rejection of the interpersonal comparisons of utility

procedure of *comparative statics* (which is based on the *ceteris paribus* method) is used:

In every problem of economic theory certain variables...are designated as unknowns, in whose determination we are interested. Their values emerge as a solution of a specific set of relationships imposed upon the unknowns by assumption or hypothesis. These functional relationships hold as of a given environment and milieu....It is hardly enough, however, to show that under

certain conditions we can name enough relations (equations) to determine the values of our unknowns. It is important that our analysis be developed in such terms that we are aided in determining how our variables change qualitatively or quantitatively with changes in explicit data. Thus, we introduce into our system certain data in the form of parameters, which in changing cause shifts in our functional relations. The usefulness of our theory emerges from the fact that by our analysis we are often able to determine the nature of the changes in one or more parameters....This in brief is the method of *comparative statics*, meaning by this the investigation of changes in a system from one position of equilibrium to another without regard to the transitional process involved in the adjustment.

[Samuelson, 1947, pp. 7 – 8]

CHAPTER 4
CRITICISMS