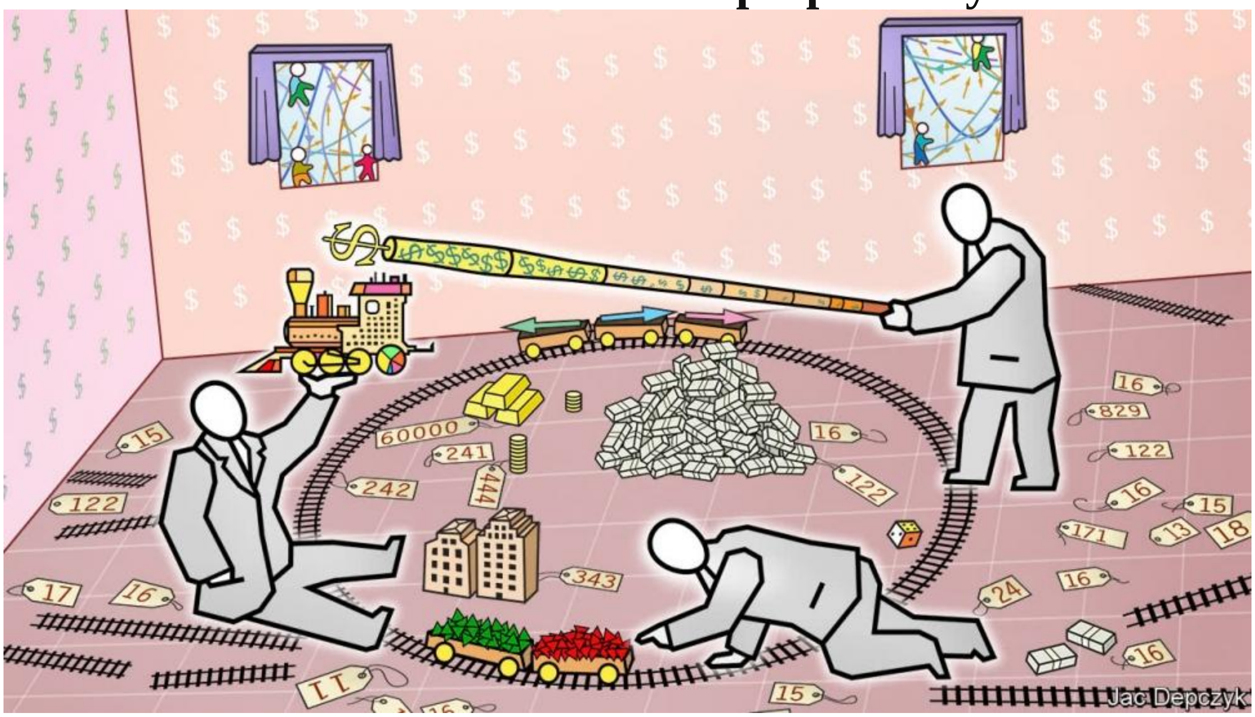
The worth of nations

Economists focus too little on what people really care about



A CYNIC, says one of Oscar Wilde's characters, is a man who knows the price of everything and the value of nothing. But, as philosophers have long known, assigning values to things or situations is fraught. Like the cynic, economists often assume that prices are all anyone needs to know. This biases many of their conclusions, and limits their relevance to some of the most serious issues facing humanity.

The problem of value has lurked in the background ever since the dismal science's origins. Around the time Adam Smith published his "Wealth of Nations", Jeremy Bentham laid out the basis of a utilitarian approach, in which "it is the greatest happiness of the greatest number that is the measure of right and wrong". In the late 19th century Alfred Marshall declared the correct focus of economics to be the "attainment and…use of material requisites of well-being". Or, as his student, Arthur Pigou, put it, "that part of social welfare that can be brought directly or indirectly into relation with the measuring rod of money".

Equating money with value is in many cases a necessary expedient. People make transactions with money, of one form or another, rather than "utility" or happiness. But even if economists often have no choice but to judge outcomes in terms of who ends up with how many dollars, they can pay more attention to the way focusing on "material well-being", as determined by the "measuring rod of money", influences and constrains their work.

The measuring rod itself often causes trouble. Not every dollar is of equal value, for instance. You might think that if two economists were forced to bid on an apple, the winner would desire the apple more and the auction would thereby have found the best, welfare-maximising use for the apple. But the evidence suggests that money has diminishing marginal value: the more you have, the less you value an extra dollar. The winner might therefore end up with the apple not because it will bring him more joy, but because his greater wealth means that his bid is less of a sacrifice. Economists are aware of this problem. It features, for example, in debates about the link between income and happiness across countries. But the profession is surprisingly casual about its potential implications: for example, that as inequality rises, the price mechanism may do a worse job of allocating resources.

Equating dollar costs with value misleads in other ways. That economic statistics such as GDP are flawed is not news. In a speech in 1968 Robert Kennedy complained that measures of output include spending on cigarette advertisements, napalm and the like, while omitting the quality of children's health and education. Despite efforts to improve such statistics, these problems remain. A dollar spent on financial services or a pricey medical test counts towards GDP whether or not it contributes to human welfare. Social costs such as pollution are omitted. Economists try to take account of such costs in other contexts, for example when assessing the harms caused by climate change. Yet even then they often focus on how environmental change will affect measurable production and neglect outcomes that cannot easily be set against the measuring rod.

Economists also generally ignore the value of non-market activity, like unpaid work. By one estimate, including unpaid work in American GDP in 2010 would have raised its value by 26% (and drawn a very different picture of the contributions of different demographic groups). As Diane Coyle of Cambridge University has argued, the decision to exclude unpaid work may reflect the value judgments of the (mostly male) officials who first ran statistical agencies. But it seems likely that economists today still treat things which cannot easily be measured as if they matter less.

Economists are at their least useful when a measuring stick should not be used at all. They have been known to calculate, for example, the financial gains from achieving gender equality. But gender equality has an intrinsic value, regardless of its impact on GDP. Similarly, species loss and forced mass migration impose psychic costs that resist dollar valuation but are nonetheless important aspects of the threat from climate change.

Such quandaries might suggest that ethical issues should be left to other social scientists. But that division of labour would be untenable. Indeed, economists often work on the basis that tangible costs and benefits outweigh subjective values. Alvin Roth, for example, suggests that moral qualms about "repugnant transactions" (such as trading in human organs) should be swept aside in order to realise the welfare gains that a market in organs would generate. Perhaps so, but to draw that conclusion while dismissing such concerns, rather than treating them as principles which might also contribute to human well-being, is inappropriate. Further, the very act of pulling out the measuring rod alters our sense of value. Though the size of the effect is disputed, psychological research suggests that nudging people to think in terms of money when they make a choice encourages a "businesslike mindset" that is less trusting and generous. Expanding the reach of markets is not just a way to satisfy preferences more efficiently. Rather, it favours market-oriented values over others.

The Pharrell Williams school

Some economists advocate the creation and use of broader measures of well-being. Several organisations, including the European Commission and the World Bank, now publish data series presenting a more comprehensive picture of social health. But the costs of the standard approach are growing. Price is a poor measure of the value of digital goods and services, which are often paid for by giving access to data. Technological progress promises to create ever more situations in which ethical considerations conflict with narrowly material ones. The question of how to increase well-being in such a world deserves greater attention.

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