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Alan Peacock

Excerpt

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ALAN PEACOCK

PUBLIC CHOICE ANALYSIS
IN HISTORICAL PERSPECTIVE

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The four *Raffaele Mattioli Lectures* were delivered by Alan Peacock at the
Università Commerciale “Luigi Bocconi” in Milano, from 5th to 7th April 1989.

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FIRST LECTURE

The Demand for Historical Perspective

1. *Introduction.* – 2. *The Fall in the Demand for Historical Perspective.* – 3. *The Scope of Public Choice Analysis.* – 4. *The Contribution of Historical Perspective.* – 5. *A Personal View of Historical Perspective.* – 6. *Concluding Remarks.*

1. *Introduction*

The Italian economist and public figure in whose memory these lectures were founded, regarded the writings of the masters of the past as a source not only of enjoyment but also of inspiration and enlightenment. I am sure that all of us have derived consumption benefits from reading the classics of the past and have our own particular favourites. In the field of public finance and public choice alone, who would not admire the penetrating, terse analysis interlarded with good humour in David Hume's essays, the breadth of vision and style of Smith's analysis of the tasks of government, the way in which Wicksell builds his analysis out of a balanced critique of the work of his forebear and contemporaries, and the audacity of Einaudi's ideas – to mention only a few writers familiar to us all? I am sure also that most of us perceive that there are external economies of production to be derived from even casual reading of the works of our forebears, in the sense that we may believe that our own output of ideas and their application benefit from avoiding what Lionel Robbins in a familiar phrase called "provincialism in time". We all enjoy, I suspect, garnishing our contributions to economic literature with a pithy quotation from "the classics", though a veneer of scholarship must not have us subjected to the charge of misplaced reverence for the past.

I could rest my case for devoting these lectures to a study of the links between past and present writings on public finance and public choice on the inspirational content of the contribution of our forebears. I do not do so, for I have no great discoveries to report, which would differentiate my product from

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those who have much greater claims to be scholars of our subject. In any case, if I did so, I suspect that I would be doing less than justice to the Mattioli tradition which I take to be the view that the study of the history of economic ideas is an essential part not only of the education but also of the training of an economist, and, what is more, requires professional economists to refer back frequently to the literature of the past. This is a much more difficult case to establish, and, although I have every sympathy with it and believe it applies in my own case, such as it is, I am not sure that I can find completely convincing arguments to support it. However, even if I would find it difficult to accept that the history of economic ideas is an indispensable piece of the equipment of a professional economist, I think that it must be included amongst the list of alternative factors within the combination of factor inputs which produce present-day output of economic ideas and their application to policy questions. I shall go further and argue that the opportunity cost of historical perspective may indeed be lower in the production of ideas about the role of the public sector in the economy, the subject matter of our disciplines, than in other fields of political economy.

In this opening lecture, I shall offer a general survey of the contemporary view of what I shall call “the demand for historical perspective”. I shall then develop my case for retaining the history of economic ideas as a significant, if not indispensable, element in the training of specialists in public finance and public choice. I shall consider the question: “is there evidence that ‘output’ has in any way suffered because of a lack of historical perspective?” Answering that question will provide me with a simple methodology which I shall use in illustrating the value of historical perspective in the analysis of public sector growth, which will form the subject of subsequent lectures.

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In my professional life, I have witnessed a remarkable shift in the demand curve for historical perspective – to the left. When I was an undergraduate, a course on the history of economic thought was the spinal column of the degree in Political Economy in Scotland and certainly an integral part of the main and specialised courses in economic theory in England. The public recognition of this phenomenon can be gauged by the question put to me by the Chief Education Officer of Scotland when I first became a full Professor in Edinburgh in 1957. He asked me: “and what is your period?” He meant, of course, who were the political economists of the past on whom I claimed to be an authority. My retrospective reply to him, given in my Inaugural Lecture,¹ was “the next ten years and beyond” and a firm statement to the effect that we do not emulate the example of Adam Smith merely by being an authority on what he wrote. My reforming zeal led me to consign the history of economic ideas to a specialised course given by an economist with little interest in research, but in my own defence let it be said that not long afterwards I did appoint a young economist who is now famous for his work in the history of ideas, Donald Winch, though he was also expected to teach international economics! What I did was typical of my generation of younger heads of department. The history of economic ideas appeared to have too high an opportunity cost as an input into the basic training of economists, though it could be taken as an optional course, useful for those who combined economics with more historically or institutionally inclined disciplines such as history and politics. As in many Anglo-Saxon universities, it was feared that it might become a haven for those less gifted in or resistant to mathematics and statistics. At the research level, there were positive dangers perceived in concentrating on the scholastic aspects of the history of ideas, as was pointed out to me at

1. ALAN T. PEACOCK, ‘From Political Economy to Economic Science’, Inaugural Lecture as Professor of Economic Science, University of Edinburgh, *University of Edinburgh Gazette*, 1957.

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the London School of Economics by my colleagues when I considered writing a Ph.D. thesis on the work of von Mangoldt. Scholarly work required roundabout methods of production, yielding returns only in the long term, and uncertain ones at that, in the sense that my peer group would regard scholasticism as a poor substitute for evidence of analytical ability. The personal satisfaction derived from discovering new facts about and presenting new insights into the works of dead men would be bought at the risk of losing promotion, remaining a junior lecturer whilst others were pushing out a stream of articles in major journals and becoming “upwardly mobile”. Being poor, married with children and somewhat risk averse, I delayed indulgence in the exploration of the past sufficiently to heed their advice. The clearest evidence of the decline of interest in and the influence of historical perspective in economics may be seen in the comparative growth of articles in economics and public finance journals on the various disciplines. “HET” now comes bottom of the list of the main specialist categories.¹

I am simply not competent to explain in detail how this remarkable change infected economics principally in Anglo-Saxon countries, and it would take me too far away from my main theme to explore the characteristics of economists’ utility functions when it comes to their perception of the factor-mix of what they produce. Two obvious explanations may be briefly mentioned both of which are associated with the perceived obsolescence of ideas from the past as a tool of the trade. The first was the manifest success of mathematical formulation of economic propositions, an activity which, it must be recalled, is as old as economics as a systematic discipline. Claiming attention for one’s competence as an economist no longer required extensive knowledge of and commentary on the work of precursors. It is clearly difficult to date the change, and it certainly did not take place simultaneously in countries noted for their contributions to economic thought. If we take public finance, Wicksell, as we have noted, clearly regarded it as necessary to stake his claim to auth-

1. See DAVID C. COLANDER and ARJO KLAMER, “The Making of an Economist”, *Journal of Economic Perspectives*, Fall 1987, pp. 95–111, for United States evidence.

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ority in economic speculation by extensive quotation from past writers, before presenting his own formulation of the principles of just taxation. His work¹ appeared, significantly enough, in German in 1896, but there is a marked change in the exposition of his follower Lindahl in which his commentary on past writers is consigned to footnotes, though, even in 1919, he writes also in German.²

The second explanation lies in the increase in the demand for economic advice as a contribution to the solution of policy problems. It is an intriguing question how far the economic analysis of “market failure” led to the supply of ideas creating its own demand, but the result which was clear enough is that the form of economic advice required economists to teach economic logic to those in charge of policy and to attempt to quantify the influence of policy measures on the appropriate economic variables, such as employment, output and prices. Placed more in the limelight of policy, the economists’ skills had to include the classification if not the collection of data, learning how to analyse the data and how to develop economic models which embodied assumptions about the influence of government policy measures. “HET” was simply crowded out by the change in the nature of the economists’ product. As I shall demonstrate, the treatment of government solely as a policy mechanism was one of the unfortunate results, a mistake which might have been avoided by an investment in historical perspective.

In my own country, however, the process went much further than the relegation of “HET” to a secondary role in the education and training of economists. In a remarkable book, the British historian J. H. Plumb³ shows how modern historians have systematically destroyed the past as having some special relevance in defining the role of a particular people or nation and the

1. KNUT WICKSELL, *Finanztheoretische Untersuchungen nebst Darstellung und Kritik des Steuerwesens Schwedens*, Jena: G. Fisher, 1896.

2. ERIK LINDAHL, *Die Gerechtigkeit der Besteuerung: Eine Analyse der Steuerprinzipien auf der Grundlage der Grenznutzentheorie*, Lund: Gleerup und H. Ollson, 1919. The relevant analysis is translated as ‘Just Taxation – A Positive Solution’, in RICHARD A. MUSGRAVE and ALAN T. PEACOCK, eds., *Classics in the Theory of Public Finance*, London: Macmillan, 1958.

3. See J. H. PLUMB, *The Death of the Past*, London: Macmillan, 1969.

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courses of action which will both ensure and sanctify its material and spiritual success. The past, so it has become fashionable to believe, has become an encumbrance in trying to understand the problems of modern society for the descriptions and analysis of past events has been surrounded by myth and dogma. A similar attempt to “kill the past” is associated particularly with the attitude of the famous Cambridge School beginning with Alfred Marshall, although the reasons differed with different members of it. Marshall was a dominant figure who was acutely jealous not only of his contemporaries but of those who may have anticipated his views. He was grudging in his praise of his forebears and extremely selective in his choice of “honourable mentions” of both his precursors and contemporaries. His contemptuous treatment of socialist economics and particularly Marx is almost pathological, and seems to have infected Keynes.¹ He seemed to have made a deliberate attempt to suppress competition from non-British economists by his influence on editorial policy of the *Economic Journal* and was furious, so it has been reported, when he discovered that Edgeworth had adopted the cowardly practice of criticising him by publishing the criticism in an Italian journal! His rationalisation of his wish to ignore the past was that one’s time should not be wasted on “the mistakes of dead men”!² Pigou’s work, *A Study in Public Finance*,³ is practically innocent of references to past work with a notable absence of any discussion of what we would today call public

1. I know that this judgment might be regarded as too sweeping, but see the important article containing the evidence by TERENCE W. HUTCHISON, ‘Insularity and Cosmopolitanism in Economic Ideas, 1870-1914’, *American Economic Review*, May 1955, pp. 1-16. Hutchison is more charitable than I am and attributes Marshall’s refusal to countenance discussion of other schools of thought involving unfamiliar concepts and expressed in other languages as a way of avoiding the “sales resistance” to economic ideas emanating from practical men of affairs whom he desired to influence. In post-Marshallian Cambridge, at least it can be claimed by the “left wing”, that they have derived continuous and deep inspiration from the works of Ricardo and Marx.

2. For a detailed examination of Marshall’s views on his forebears and contemporaries, see *The Early Economic Writings of Alfred Marshall, 1867-1890*, edited and introduced by JOHN K. WHITAKER, London: Macmillan, 1975, vol. 1, Chapter 1.

3. ARTHUR C. PIGOU, *A Study in Public Finance* (1928), Third edition, London: Macmillan, 1947.

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choice problems which had already appeared in the Italian and Swedish literature.¹ Keynes presents a curious paradox. In his earlier writings he specialised in the production of vignettes on such economists as Jevons, Ricardo and Marshall himself which are sympathetic, but his attack on classical macroeconomic theory is wholly misplaced and his search for companionship with “the economic underworld” of Major Douglas, Silvio Gesell and J. A. Hobson verges on the grotesque.² In Keynes’s case, “cocking a snook” at the past was a fashionable sales technique used by his Bloomsbury friends, such as Lytton Strachey, and clearly not designed to be taken entirely seriously. He was quite capable at looking for allies amongst his forebears on a selective basis, notably in ingratiating himself with his French colleagues by the claim that his views on the rate of interest had an affinity with those of Montesquieu!³ It would be absurd to argue that the upshot of this cavalier treatment of the history of ideas, particularly ideas from other countries, produced some form of intellectual paralysis in Anglo-Saxon thinking. On the contrary, the Ricardian-Marshallian tradition of analysis with its emphasis on problem solving is, as we are all aware, one of the most important contributions to economics. No doubt there has been a parallel neglect of this tradition in other countries, particularly in those countries where analytical relativism held sway, that is to say in countries such as Germany where generalisations in economics were claimed to be conditioned by the problems of a particular era. The fact remains, however, that the Cambridge tradition, which was enormously influential in the field of public finance in Anglo-Saxon countries, was characterised by a distinct

1. Blaug records that Pigou, when asked to review a work on the history of economic thought, replied: “These antiquarian researches have no great attraction for one who finds it difficult enough to read what is now thought on economic problems, without spending time in studying confessedly inadequate solutions that were offered centuries ago”. See MARK BLAUG, *Economic Theory in Retrospect*, Fourth edition, Cambridge: Cambridge University Press, 1985, p. 1.

2. See JOHN MAYNARD KEYNES, *The General Theory of Employment, Interest and Money* (1936), reprinted in *The Collected Writings of John Maynard Keynes*, vol. vii, London: Macmillan, 1975, Chapter 23.

3. See KEYNES, ‘Preface to the French Edition’, in *The General Theory of Employment, Interest, and Money*, *op. cit.*, p. xxxv.

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neglect of governmental institutions as a suitable subject for analysis. Marshall's natural caution led him to be very careful about the claims of economic analysis in identifying policy measures, even before any consideration which might have been given by him to how such measures might be implemented. In the field of public finance, for example, he is noted for his famous proposal that collective satisfaction could be increased if increasing cost industries were taxed and the proceeds used to subsidise decreasing cost industries, but he makes a number of important reservations about the possibility of translating such a proposal into positive action.¹

The interesting case, naturally, is that of Keynes. He was clearly much more confident about what governments should be doing, as witness his enormous output of policy recommendations culminating in the famous last chapter of the *General Theory*. He had also a great deal of practical experience within government in both World Wars. Yet he was imbued with what public choice theorists, such as Buchanan, Burton and Wagner² and latterly Rowley,³ have labelled the "Harvey Road mentality", kindred intellectual spirits who believed that the United Kingdom should and would be governed by an intellectual aristocracy, namely themselves, who could persuade the public and politicians to follow their prescriptions. This presupposed, in Keynes's case, that functional finance was largely a question of knowing which policy instruments to choose and what their quantitative effects would be on relevant policy variables, such as aggregate expenditure and its components. This approach contains two cardinal errors. It assumed that private sector decision makers reacted purely passively to government measures and were incapable of learning how to adjust their actions. It assumed that even if the behavioural assumptions regarding the

1. See ALFRED MARSHALL, *Principles of Economics* (1890), Ninth (Variorum) edition, Edited by W. CLAUDE GUILLEBAUD, London: Macmillan, 1961, vol. 1, Book v, Chapter XIII.

2. See JAMES M. BUCHANAN, JOHN BURTON and RICHARD E. WAGNER, *The Consequences of Mr. Keynes*, London: Institute of Economic Affairs, 1978.

3. See CHARLES K. ROWLEY, 'John Maynard Keynes and the Attack on Classical Political Economy', in JAMES M. BUCHANAN, CHARLES K. ROWLEY and ROBERT D. TOLLISON, eds., *Deficits*, Oxford: Blackwell, 1987, pp. 115-22.