Economics without Preferences

Economics without Preferences lays out a new microeconomics – a theory of choice behavior, markets, and welfare – for agents who lack the preferences and marginal judgments that economics normally relies on. Agents without preferences defy the rules of the traditional model of rational choice but they can still systematically pursue their interests. The theory that results resolves several puzzles in economics. Status quo bias and other anomalies of behavioral economics shield agents from harm; they are expressions rather than violations of rationality. Parts of economic orthodoxy go out the window. Agents will fail to make the fine-grained trade-offs ingrained in conventional economics, leading market prices to be volatile and cost-benefit analysis to break down. This book provides policy alternatives to fill this void. Governments can spur innovation, the main benefit markets can deliver, while sheltering agents from the upheavals that accompany economic change.

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Microeconomics and Policymaking Beyond the Maximizing Individual

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Preface

Economics without Preferences explores the theory of markets and economic behavior when individuals cannot form the preference judgments and marginal trade-offs taken for granted in economics. Books on economic theory have fallen out of fashion, particularly when they consider competitive markets and prices. With the exception of textbooks, the few still published tend to be technical monographs. This book addresses the entire community of economists – from behavioral economists to decision theorists to welfare economists to general equilibrium theorists – and shows how the absence of preferences recasts each of these areas.

Once upon a time, each generation of economic theorists told the story of how they had superseded the past – from Marshall in the *Principles of Economics* to Samuelson in his triumphant excursions into the history of economic thought. Everything they could say we can say better. This pattern came to a halt as the study of markets turned from theoretical fundamentals to extensions and applications, often in outlying fields such as public finance or macroeconomics. More recently, an avalanche of behavioral evidence has buried the neoclassical theory of the rational consumer and has launched new fields – behavioral and experimental economics – but it has not led to a new chapter in the 200-year history of the economic theory of value. I will therefore retell the story of how equilibrium and decision theory have developed through the last century; the tale explains why the present difficulties of microeconomic theory arose and how to overcome them.

In the clash between the classical theory of rationality and the evidence of behavioral economics, this book aims for reconciliation. The first article of the proposed settlement argues that the classical theory's claims of rationality are unjustified; much of the dispute between orthodox preference theory and behavioral economics then dissipates. The second article will show that many putative violations of rationality not only do agents no harm but are in fact evidence of a deliberate pursuit of self-interest.

The agents in this book will always be able to form some preference judgments. Orderings come readily when agents are offered a good deal – if for example the terms of trade are tilted in their favor – or when they can reduce a complex decision to simple elements that they do know how to weigh. But agents often do not come to judgment nor do they have a reason to do so. Agents still of course have to make choices. The book's title skips over these nuances. But the more precise alternatives – *Economics without some of the preference judgments normally assumed* or *Economic theory with incomplete and nonsmooth preferences* (the latter an actual suggestion) – were worse. A title closer to the mark would underscore the absence of marginal preference judgments, the cornerstone on which prices and social decision-making are ordinarily built.

Theorists who have read the manuscript conclude that it targets a general readership, nontheorists consider it a book of mathematical economics. Although the issues I discuss are not inherently of great mathematical complexity, their treatment in economics has been thoroughly mathematicized and I must engage those analyses. The problems of how to speak to theorists and nontheorists and how to combine text and formal modeling have no obvious solution. I have aimed for a Switzerland that both parties can enter peacefully rather than a demilitarized zone where no one will tread comfortably.

The lion's share of comments on the ideas herein came while I presented and published the 15 or so interrelated papers I wrote in anticipation of this book. It would be difficult to exaggerate how much I learned in the process and I will not try to summarize those debts. I am delighted however to thank Sophie Bade, Duncan Foley, Daniel Kahneman, M. Ali Khan, Mark Steitz, Chris Udry, Peter Wakker, and a clear-sighted anonymous reader for detailed comments on several chapters. My initial discussions with Andreu Mas-Colell were indispensable. Finally, I thank Patricia Craig for her patient sifting between plausible and misguided ideas for a book cover and the British Academy for financial support.