

Lionel Robbins:

**Ogre
or
Prophet?**

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1 Introduction

When I first joined LSE as a naive mathematician, Lionel Robbins was at the zenith of his career. I recall him standing before the fire in the Senior Common Room, holding an audience of acolytes spellbound while he put the world to rights. At the time, I thought he was an ogre. It is only now when I reflect upon his writings and the intellectual environment in which he wrote that I recognize that he also deserves his reputation as a prophet.

For example, his famous definition of economics in terms of the allocation of scarce resources seems trite to modern ears (Robbins [5, p.15]). How else should economics be defined? But such an attitude neglects Robbins' part in beating the drum for the newly emergent discipline that we now call neoclassical economics.¹ It is only because prophets like Robbins preached so successfully that we now regard the mistakes to which he was reacting as unthinkable.

On the other hand, his dismissive attitude to bread-and-butter quantitative work comes across as hopelessly old-fashioned. Ariel Rubinstein's [7] recent Presidential Address to the Econometric Society shows that there is still at least one leading economist who shares Robbin's view that the proper role for economists is to tell insightful stories on a grand scale, but most of us now regard economics as a science capable of making accurate predictions in favourable circumstances.

However, I shall explore neither of these issues any further, because other contributors to this conference will do it better. Instead, I shall examine two other issues on which Robbins expressed strong opinions.

The first issue to be explored is Robbins' attitude to the theory of revealed preference, on which subject he was an ogre. If he had understood the possibilities of the theory better, he wouldn't have been so ready to condemn welfare economics on the grounds that interpersonal comparisons of utility are economically meaningless (Robbins [6]).

On the second issue, I think he was a prophet, albeit of the type who cries in the wilderness. His insistence that economics should be separated from both psychology and moral philosophy is a lesson that modern economists would do well to heed. It is not our business as economists to instruct politicians on what social welfare function they should be operating. Nor are we justified in insisting that

¹Robbins is commonly said to have been a member of the Austrian school of economics. He certainly liked to quote in German, but the lessons he draws from the early work of von Mises and others seem purely neoclassical to me.

the optimizing paradigm which lies at the heart of our discipline must apply to psychological data, as in much modern behavioural economics (Robbins [6]).

2 Revealed Preference

Jeremy Bentham's adopted the term *utility* as a measure of the pleasure or pain a person feels as a result of a decision being made. Perhaps he thought that some kind of metering device might eventually be wired into our brains that would show how many units of utility we are experiencing. This is a less bold hypothesis than it may once have seemed, since we now know that rats will pull a lever that activates an electrode embedded in a pleasure center in their brains in preference to anything else whatever—including sex and food. It is therefore unsurprising that a modern school of behavioural economists have reverted to this classical understanding of the nature of utility. A more specialized group devote their attention specifically to what they call happiness studies. However, the theory of revealed preference remains the modern orthodoxy in economic theory.

The theory of revealed preference goes back a long way. Thomas Hobbes, for example, sometimes writes as though choosing a when b is available is unproblematically the same as liking a better than b . Its modern incarnation is usually thought to have been honed to perfection by Paul Samuelson, but the idea was on the table in Robbins' heyday.

Its history is worth recalling. Economists after Bentham became increasingly uncomfortable with the naive hypothesis that our brains are machines for generating utility. They therefore made efforts to avoid appealing to the idea, which turned out to be very successful in the context of perfectly competitive markets. The eventual result was an intellectual turn-around known as the Marginalist Revolution in which results were obtained without asking that economic agents do more than rank the alternatives available to them (without any need to say by how much they prefer one alternative to another).

Robbins [5] seems to have boarded the marginalist bandwagon in his formative years, but never to have appreciated the value of taking the further step of seeking to eliminate *all* psychological explanations of human choice behaviour from economic theory. He seems not to have seen that the pure theory of revealed preference makes it possible to carry through his ideal of separating economics from psychology by eliminating *all* assumptions about the psychological causes of our choice behavior. Instead of appealing to psychological explanations, the pure theory assumes that we already know what people choose in some situations, and uses this data to deduce what they will choose in other situations.

For example, Alice may buy a bundle of goods on each of her weekly visits to the supermarket. Since her household budget and the supermarket prices vary from week to week, the bundle she purchases isn't always the same. However, after observing her shopping behavior for some time, one can make an educated guess about what she will buy next week, once one knows what the prices will be, and

how much she will have to spend. The accuracy of such a guess, of course, depends on the extent to which Alice's choice behaviour is both stable and consistent.

With some mild assumptions, acting consistently can be shown to be the same as behaving *as if* seeking to maximize the value of something. Whatever this abstract something may be in a particular context, economists call it utility. However, this modern notion of utility doesn't have the same explanatory role as the classical notion.² In the modern theory, it isn't true that Alice chooses *a* rather than *b* because the utility of *a* exceeds the utility of *b*. On the contrary, we make the utility of *a* larger than the utility of *b*, because Alice chooses *a* rather than *b*.

My guess is that Robbins, like many authors today, regarded revealed preference theory as a not-very-interesting methodology for *discovering* an agent's rankings over economic alternatives, rather than as a philosophical alternative to treating psychological rankings fundamental to economic theory. As a consequence, he failed to appreciate the importance of the work of Von Neumann and Morgenstern on making rational decisions in risky situations. He therefore found himself denouncing cardinal utility functions³ long after Von Neumann and Morgenstern had shown how a meaning can be attached to them without any need to venture into metaphysics or moral philosophy.

His animosity to cardinal utility belongs in the same bag as his hostility to the idea that utilities can be compared between different individuals. It is certainly true that we don't know how to compare Alice's happiness or pain with Bob's happiness or pain. We can watch their behaviour in the dentist's chair, but who is to say how this relates to what they are experiencing in the privacy of their own skulls? Comparing classical utilities therefore remains problematic, and if welfare economics had to be judged on whether a sound economic theory of interpersonal comparison of classical utility were available, I would agree with Robbins that the issues would all need to be delegated to moral philosophy.

However, John Harsanyi [4] showed that we don't need to compare *classical* utilities across individuals to construct a viable theory of welfare economics. We just need to follow Von Neumann and Morgenstern further down the revealed-preference road. Not only can we thereby obtain a theory in which Von Neumann and Morgenstern utilities are compared across individuals, but we can also create a version of utilitarianism that isn't vulnerable to the foundational problems that are commonly thought to have wrecked Bentham's attempt.

On the subject of the interpersonal comparison of utility, I therefore think that Lionel Robbins was a genuine ogre, whose authority served to hinder progress for many years. Indeed, it is only recently that it became impossible to hear microeconomics students in one class being taught that interpersonal comparison of utility is meaningless, while students in the classroom next door were simultaneously being

²Much confusion could be avoided if we adopted Bentham's own suggestion of referring to classical utility as *felicity* and reserving the word *utility* for the modern usage.

³Ordinal utility functions were fine with Robbins because they are only used to describe a ranking. A cardinal utility function attaches a meaning to the amount by which the utility of one alternative exceeds the utility of another.

taught to take interpersonal comparison for granted while studying welfare economics.

3 Wearing One Hat at a Time

Robbins felt that one should only wear one hat at a time. We are as entitled as any other citizen to hold our own views on politics, human psychology or morality, but it is unprofessional to allow our views on subjects outside economics to influence our analysis of an economic problem.

In advising various governments on how to organize big-money telecom auctions, I consciously asked myself what Lionel Robbins would say when it was repeatedly put to me that deciding the trade-offs between various governmental objectives was a technical problem rather than a political problem. Without his authority and that of others like him, I don't think I would have had the confidence to insist that determining social welfare functions is the responsibility of politicians rather than economists.

There is room in this paper for only two brief examples, one that is arguably moral in character and the other psychological.

The Stern report. The Stern [5] report on the economic implications of global warming has been very influential, but it would have carried even greater weight without the infighting that followed its publication among various economic experts about whether the report used the "correct" discount rate when assessing the future under various contingencies. I understand that the political impact of the report might have been lessened if it had been complicated in the way I propose below, but I think Lionel Robbins would have approved of the suggestion.

I think Robbins would have said that it isn't the business of economists to propose a "correct" social discount rate. If it is meaningful at all to speak of a correct rate, we should leave this to moral philosophers or other pundits whose specialities lay claim to expertise in this area.

Instead of using a specific discount rate that would inevitably be controversial (because a great deal hangs on whether the rate is relatively large or small), I suggest that there would have been a case for presenting the calculations for the whole range of discount factors that anyone thinks reasonable. Attention could then have been directed at the implications of insisting on one discount rate rather than another. To critics who argue that it isn't worth spending a large sum now to ameliorate some climatic trend because we ought to discount the future heavily, one could then respond by pointing to the realities of the gambling game we would then be forcing our children or our grandchildren to play. One might thereby hope to achieve some consensus on what discount rate is genuinely politically viable, rather than arguing in the abstract about a concept whose implications are hard even for experts to evaluate.

More generally, when clients find formulating a social welfare function too abstract a task, they can be asked for their preferences over a variety of concrete scenarios. Economic theory can then be used to point out any inconsistencies in the expressed preferences and then to summarize the results in terms of a social welfare function where possible.

Inequity aversion. Robbins [6, p.151] was particularly anxious to separate economics from psychology. Would that he were alive today to stem the excesses of the radicals from the behavioural school of economics, who insist on fitting utility functions to psychological data as though neoclassical economics could always be expected to explain everything, while simultaneously proclaiming that they are refuting neoclassical economics!

I share the view of nearly all real psychologists that it is a mistake to think that the optimizing paradigm can be successfully applied across the board to all human behaviour. For example, very few laboratory experiments fail to show evidence of learning when the opportunity is offered. The subjects' choice behaviour then changes over time. So it can't be modeled as maximizing a utility function unless the proposition is tautologized by making utility a function of time (Binmore [1]).

The response that empirically derived utility functions which exhibit "social preferences" actually work in practice doesn't bear examination. Fehr and Schmidt's theory of inequity aversion is the jewel in the crown of those who take this line. According to the theory, an agent's utility function is characterized by two parameters: α measures the agent's envy at being poorer than others; β measures the agent's discomfort at being richer. In an invited lecture given at the 2003 World Congress of the Econometric Society, Fehr and Schmidt [3, p.222] say:

Using the data that is available from many experiments on the ultimatum game, Fehr and Schmidt calibrate the distribution of α and β in the population. Keeping this distribution constant, they show that their model yields quantitatively accurate predictions across many bargaining, market and co-operation games.

However, it is logically impossible to calibrate α and β using ultimatum game data. They don't keep the distribution of α and β constant, but feel free to alter the distribution when "predicting" new data. Even so, the "predictions" are so far from accurate that they can arguably be regarded as refuting their theory (Binmore and Shaked [2]).

In criticizing this kind of scientifically irresponsible work, I am not arguing that experimental economics is a waste of time. I am totally sold on the idea that economic theories should be tested in the laboratory under carefully controlled conditions. When they don't work when they should, we ought then to try to revise the theory. But nothing is to be gained by forcing human psychology into an economics shoe by adding extra parameters to the theory when the foot doesn't fit, or by pretending that the foot fits when it doesn't. When we enter a psychological laboratory, we should leave our economic prejudices at the door.

4 Conclusion.

Lionel Robbins was both an ogre and a prophet. To quote a forgotten nursery rhyme: When he was good, he was very, very good; but when he was bad, he was horrid. I suppose the same could be said of all great men.

Robbins combined the kind of authority that comes from a supreme confidence in knowing how things should be done with an integrity that was totally transparent. They don't make them like that any more.

5 References

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