Review: [untitled]
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   The Costs of Economic Growth. by Ezra J. Mishan
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Bank monthly review, is followed by sharply critical studies by Brunner and Meltzer and the Federal Reserve Bank of St. Louis, then turns to research on the prime rate by the Federal Reserve Bank of New York, and concludes with a pair of defensive speeches given in 1966 by the governors mentioned above.

Each section begins with a very brief introduction and concludes with short lists of very global "questions for further study" and "suggested additional readings," most of them entire volumes. Further, the appropriate chapter numbers in 14 current textbooks in money and banking are keyed to the seven sections of readings.

With so few readings for each topic, it would be an easy game to find fault with the editor's choices and to suggest additions and substitutions. However, this reviewer chooses not to play. The editor has done a competent job, within the constraints of space and coverage, of assembling a collection of intelligible, instructive, and provocative readings, which should be useful in any standard economics course in money and banking.

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Do not be misled by the title of Ezra Mishan's engaging book. You might have expected him to argue that our economic institutions are too patient—that we should save less so as to enjoy greater consumption today. Not that this sort of argument is absent from the book. In Mishan's hands it goes something like this: There are probably more disamenities associated with investment (smoke and noise and so forth) than are associated with consumption; consequently, the apparent social rate of return to investment is highly exaggerated, and therefore under a rational social calculus, resources should be shifted from investment to consumption.

Of course, Mishan realizes that the composition of investment and consumption are of overriding importance. I could easily imagine that Mishan would oppose an increase in automobile production at the expense of, say, hospital construction. The construction of hospitals is normally classed by economists as investment, whereas automobiles are usually thought to be consumption goods. It is not that Mishan is an antigrowth-man in this very technical sense. I cannot say with assurance how much below the Golden Rule level he would favor as a target for the long-run capital-labor ratio.

It seems to me that the argument is with "growth" in a more popular sense of the word. For "growth," Americans could read the highway engineer's "progress" or the military-industrial-academic complex's "political or international necessity." The message of the tract is well summarized on the dust jacket: "As the carpet of increased choice is being unrolled before us by the foot, it is simultaneously being rolled up behind us by the yard."

There is no doubt that the author's observations are correct and pose a serious challenge. Why do we put up with noise and smoke and the destruction of our cities by highway planners? Not only do our governments make important errors of omission in not dissuading the private sector from befouling our environment, but also and more importantly government activities in themselves through highway-building agencies and others are probably responsible for some of the greatest disamenities in contemporary society. It is difficult to look to government for leadership in abatement of pollution when that same government is spending billions to create a supersonic
transport—an enterprise which provides so many disamenities that it should be
cancelled even if its budgetary costs were zero.

The book is divided into three parts. Part One, on growthmania, the no-choice
myth, and the choices open to us, is really quite excellent as far as it goes. This is the
brilliant student of the agnostic contemporary welfare economics at his very best.
He cuts through the myths of "growth," "political and international necessities," and
"progress" to remind the policy-maker that after all there is freedom of choice in this
world. In this respect, there is even much in common between the student of welfare-
economic theory and many of the practitioners of the New Politics in the United
States. Step One in the argument is to remind us that we do have freedom to shape our
lives and environment. Why do you say we must build more parking garages? Why not
instead raise the fees for parking? Or raise the gasoline tax? Or ban private auto-
mobiles from the center city?

Mishan is just very good at debunking the no-choice myth. This myth is probably
more widespread and more pernicious in America than ever was the myth of the
balanced budget. Indeed, I measure the success of the elementary course in economics
by whether or not the student has learned to appreciate that society can and does
make choices.

On the other hand, I would have preferred to see more economic history and studies
of contemporary institutions in Part One. Who is responsible for these highways, auto-
mobiles, airports, and supersonic transports? Why are highway builders so successful
in the political arena? How should we redesign our political institutions in order to
improve the quality of the resulting choices? I am not wedded by any means to the
concept of historical necessity, but I do think that before a fundamental change
occurs in America's road-building policy one might consider making a fundamental
change in, say, the Bureau of Public Roads.

Part Two is about external economies and particularly external diseconomies. It
begins with a digression on the rationale of marginal-cost pricing. There are separate
treatments of external diseconomies and property rights, external diseconomies of
built-up areas, external diseconomies and separate facilities, and external diseconomies
and social conflict. In this part, Mishan demonstrates quite clearly that he is the
master of a widespread method in welfare economics. The method is based on the
Fundamental Theorem of Welfare Economics: If certain convexity assumptions are
met (which need not detain us here) and in the absence of external economies or
diseconomies, a competitive equilibrium allocation is also a Pareto-optimal allocation.
Practitioners of this method examine an economic situation in which external economies
or diseconomies are notably present. The next step is to redesign on paper the political
and legal institutions to account for these economies or diseconomies. This is often
excellent common-room sport for academic economists and forms the basis of some
very good graduate examination questions. The results of this activity are often
extremely ingenious, but (I will argue) often beside the point.

A model is after all merely an abstraction from reality. A model is relevant only
as long as it captures the "essential" features of the real world. Abstracting for the
moment from the very great difficulties posed by the undesirable distribution of wealth,
the Fundamental Theorem of Welfare Economics serves as a useful guide to social
policy in a context in which externalities are exceptions rather than commonplace
occurrences. But external disamenities are just everywhere in the contemporary
American city. External disamenities are the rule not the exception. In the common-
room, we can consider the possibility of conferring property rights on clean air, clean
water, and peace-and-quiet. But in reality, enforcement costs required for protecting
such property rights must be staggering. Since the Fundamental Theorem of Welfare
Economics has precious little to tell us about a society in which the administration of justice and protection of property rights are costly, we are left without a paradigm for public policy.

I think that economics is in need of an essentially new paradigm to replace or augment the model which forms the basis of the Fundamental Theorem. The new model should reflect the fact that administration of any system of charges for use of facilities is in itself costly. While toll booths on every congested corner would lead to allocative efficiency in the old sense, it is quite clear that costs of administration would be ridiculous. All things considered, the gasoline tax may not be such a terrible allocative device after all. In addition, the new model should have interesting implications for the Theory of Public Goods. Indeed, is there any good which is inherently public, or is the public quality of a good merely the reflection of the face that alternative forms of allocating that good may be very costly indeed?

"Part Three hazards an incursion into those costs of industrial progress that do not lend themselves to formal analysis but are an essential part of the agenda in any enquiry concerning the social value of economic growth." Included in this part are sections on the myth of consumers' sovereignty, institutional constraints on choice, and the weak link between expanding choice and welfare. This part could be taken as an attack on the fundamental notion that expanded choice leads to improved individual and social felicity. More is not necessarily better. In this Freudian age, it is extremely difficult to disagree with this hypothesis. One does not need Galbraith's "revised sequence" to realize that Mustangs, Cougars, Virginia Slims, and Alka Seltzers are not the stuff that goes into our usual interpretation of the Fundamental Theorem and its related world-view. Nonetheless, I find many of Mishan's specific proposals for the better life not very much to my liking. I guess he is just more of a Platonist than I am.

While this matters little to the general argument, I would like to record a few of our differences with regard to specific proposals. I guess Mishan overrates the virtues of artisan work. While I see no great virtue to work per se, I might find the pill of industrial labor worth it if mixed with sufficient doses of consumption and leisure. It does not depress me as it depresses Mishan that the Church is in disarray. Nor do I find Mishan's notions of the proper sex life more attractive than those of our Madison Avenue society.

This volume should be required reading for government bureaucrats. It is also good medicine for all professional economists, particularly for "growthmen," applied welfare economists, and "hard-nosed pragmatists."

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Business Finance and Investments


This book is not really about investment decision-making, as one would suspect from the title, nor is it a programmed text as one might suspect from the publisher's name. Instead, it is merely another descriptive investments primer, of which there have been many; and in this sense it breaks no new ground, although since the mid-1950's business-school textbooks have become much less descriptive and much more analytical in content. In view of this trend, one would be entitled to expect that in