

Review of “The Hesitant Hand: Taming Self-Interest in the History of Economic Ideas”

by

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***The Hesitant Hand: Taming Self-Interest in the History of Economic Ideas.* By Steven Medema, Princeton University Press, Princeton, 2009. \$35.00 ISBN 978—0-691-12296-0**

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There are far too few nuanced accounts of economic policy, so Steven Medema's *The Hesitant Hand: Taming Self-Interest in the History of Economic Ideas* is a welcome addition to the economics literature. It should be widely read and discussed. The essence of Medema's argument is that economists have been much more nuanced in their use of the invisible hand theorem as a guide for policy than is often understood. His argument is that good economists have always been arguing that economic theory does not tell us that the market is the preferable method of organizing the economy. Instead, good economists have been making a "least worst" practical argument for laissez-faire and the market: When you consider the alternatives, based on historical considerations, the market tends to be a better way to organize economies than alternative methods. His book shows that when you read past economists, you will find that that is their view.

The book consists of a prologue, seven chapters and a short epilogue. The prologue serves as an introduction to the book. It points out that "nearly all of the economic literature prior to the later eighteenth century expressed significant qualms about the effects of self-interested behavior on social welfare and held out state intervention as the only means to mitigate these problems." (p 3) The first three chapters

develop this theme. Chapter 1, “Adam Smith and His Ancestors” follows the standard history of thought approach; it begins with a discussion of Plato and Aristotle’s views, the Scholastic’s views, the physiocrats and mercantilist view and then discusses Adam Smith’s views. Medema points out that Smith was not a doctrinaire advocate of laissez-faire, and that while Smith had an inherent suspicion of the ability of government to manage economic affairs properly, he also saw a role for government. Medema writes “Smith considered the link between private and social interests practical and imperfect, but he was also of the mind that self-interest, properly channeled, tended to engender positive results, rather than negative ones, and that government interference with its operations in the economic sphere would generally lead to inferior results.” (25)

Chapter 2, “Mill, Sidgwick and the Evolution of the Theory of Market Failure” looks at the development of classical thinking on laissez faire and policy and how it evolved after Adam Smith. He discusses Bentham’s utilitarianism, along with that of Mill and Sidgwick, pointing out that reformist nature of economic thinking of the time. Medema writes “On the whole, however, classical political economy evidences a relatively pragmatic view of the economic role of government, one borne of the utilitarianism that underlay the approach of many of the classical writers.” (30) He quotes J.E. Cairnes’s that “the maxim of laissez-faire...has no scientific basis whatever.” (31) He then proceeds to provide a nice discussion of Mill and Sidgwick’s views, presenting Sidgwick as the transition figure between Classical and neoclassical views that developed in the writings of Marshall and Pigou.

Chapter 3, entitled “Marginalizing the Market” looks at the evolution of the textbook Pigovian tradition that developed from Marshall. In it Medema points out that

while Marshall and Pigou were very hesitant about claiming any theoretical foundation for laissez-faire, and can be seen as embodying the Mill-Sidgwick Classical tradition, the work following Pigou—which might be called the Pigovian legacy, did not. The themes in these three chapters are followed up in Chapter 5, “Coase’s Challenge”. The chapter explores the limitations of the theoretical argument for laissez faire, and argues that work following Pigou, with its emphasis on externalities, concentrated on exploring limitations of the theoretical argument for the market and for laissez-faire. Medema nicely presents Coase’s critique of the entire externality framework, arguing that Coase’s argument takes us back to the Classical Mill and Sidgwick framework, of which Marshall and Pigou were a part, but which the Pigovian tradition departed from. These chapters make a coherent whole and fit nicely together

A Public Choice Theme

Chapter 4, “Marginalizing Government” seemed to me to be a bit of an interlude in the story. It discusses the Italian public finance tradition and Knut Wicksell’s work on social choice. Both of these traditions are important to public choice theory, but they are quite distinct from the history of the neoclassical social welfare tradition that was the focus of the first three chapters. Chapter 4 is followed up by Chapter 6, “Marginalizing Government II”, which explores the rise of public and social choice analysis, concentrating on public choice analysis. Combined, these two chapters provide a nice history of the public choice society and of the rise and fall of the Virginia school.

Law and Economics

Chapter 7, “The Coase Theorem and the Evolution of Law and Economics,” explores the law and economics movement which evolved out of the work of Coase. Medema presents law and economics as an “accidental byproduct of Coase's analysis” (190), the economic imperialism that accompanied it, and the Chicago school approach of Becker and Stigler. The book concludes with a short epilog “Everywhere, Self-Interest?” which argues the pendulum of views on the relationship between self-interest, market and state swings back and forth, and can be expected to continue swinging in the future.

Assessment

As should clear from what I have written, there is much that I admire in this book. I think the story Medema tells about Classical economists carefully limiting theoretical claims for the market is absolutely correct. I also agree with his presentation of Coase as being a much larger critique of welfare economics than what is found in the Coase theorem. I also find his presentation of public choice as insightful. My only complaint is that the two different subjects he addresses do not quite fit together for me. Public and social choice is outside the Pigovian tradition, and the movement to it seemed jarring. By focusing on that tradition, central parts of the Pigovian tradition story do not get mentioned. These include the work leading to the textbook Pigovian legacy (such as Abba Lerner's *Economics of Control* and the socialist calculation debate of which that was a part), and the development of macroeconomics that created a whole new foundation for government policy analysis. Neither of these get a mention in the book, even though, in my view, they played a central role in the evolution of thinking about government policy and fit more closely with the theme in the first four chapters than does public and social choice. That complaint notwithstanding, I strongly encourage anyone

interested in thinking about economists and government policy read this book; it gives a much better sense of how economists should think of policy analysis than just about any textbook.