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Essais critiques / *Review Essays*

Normative Economics Without the Concept of Preference

Review essay on:

Robert Sugden, *The Community of Advantage. A Behavioural Economist's Defence of the Market*, New York: Oxford University Press, 2018, 352 pages, ISBN 978-019882514-2

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Over the past two decades, a growing literature of behavioural welfare economics has become the mainstream view of how behavioural economics should reinterpret normative economics. While behavioural economics documents many cases where individuals deviate from well-ordered preferences—such as loss aversion, limited attention, overconfidence or framing effects—there is a consensus in behavioural welfare economics about taking the satisfaction of individuals' preferences that are not distorted by cognitive biases to be the proper normative criterion for evaluating individuals' states. The main idea of this consensus is that since individuals may be affected by cognitive biases, their judgments over what makes them better off can be distorted; hence their actual preferences cannot reasonably indicate their well-being. One proposition endorsed by behavioural welfare economics is that normative analysis should not take into account the preferences that individuals would reveal in their choices, but instead their underlying latent or "true" preferences on which they would have acted, had they not been affected by cognitive bias-

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This review essay is the product of regular discussions I had about *The Community of Advantage* with Francesco Guala during the last quarter of the year 2018 at the University of Milan. I am thankful to him for his remarks on my comments on the book. I am also grateful to Cyril Hédoin and Pierre Van Zyl for their careful reading. All mistakes remain exclusively mine.

es. In *The Community of Advantage*, Robert Sugden challenges this proposition. The author is an eminent behavioural economist who is currently professor of economics at the University of East Anglia. His book is a systematisation of his contributions over the last few decades to behavioural economics, welfare economics, social choice and philosophy of economics with one purpose in mind: laying the foundations of an alternative form of normative economics in response to the central issue he sees in the program of behavioural welfare economics—that the assumption of individuals having true preferences is unwarranted. Sugden aims to show that there is a way of developing normative economics that is compatible with the empirical findings and the theoretical refinements of behavioural economics without needing to assume that individuals make "wrong" decisions because they fail to satisfy the axioms of rational choice. His proposal is to break away from the normative criterion of preference-satisfaction and replace it with the normative criterion of opportunity. According to this criterion, individuals' interests are better served when they can choose from a larger rather than a smaller opportunity set, irrespectively of what their preferences are. The title of the book is a concept taken from John Stuart Mill's *Principles of Political Economy* that refers to the competitive market "as a network of mutually advantageous relationships" (1). Through this concept, Sugden sees cooperation for mutual benefit as a governing principle of social life, where it is for each individual to judge what counts as his/her own benefit. His ambition is to maintain the liberal tradition of political economy by developing the understanding of the market as a domain of life where each party can voluntarily agree to participate in a transaction from which they mutually expect to benefit. This book articulates Sugden's contributions (including those with his co-authors) of the last few decades in a unified system that shows that normative economics can be viable without seeking to satisfy individuals' preferences, but seeking to increase their opportunities to engage in mutually beneficial transactions.

1. Sugden's Reconstruction of Normative Economics

After an introduction on how the liberal tradition of normative economics is challenged by behavioural welfare economics and particularly by libertarian paternalism (Chapter 1), all the other chapters are written in response to four main questions. To whom should normative economics be addressed? (Chapters 2 and 3) What is the issue with behavioural welfare economics regarding its assumption of individuals having underlying true preferences? (Chapter 4) How to develop a form of normative economics that does not use the concept of preference? (Chapters 5, 6, 7 and 8) What does this form of normative economics have to say about the moral status of market relationships? (Chapters 9, 10 and 11)

Chapter 2 criticises both behavioural and neoclassical welfare economics for taking the viewpoint of a single person, who is not any of the individual members comprising the society that is being assessed. Sugden calls this view "the view from nowhere", borrowing Nagel's (1986) terms that characterise the view we should presumably take when we try to engage in moral reasoning. The "view from nowhere" is the first target of Sugden's criticism, especially when combined with the claim that the social planner should be an impartial and benevolent spectator when assessing individuals' well-being.[1]

In response to the "view from nowhere", Chapter 3 proposes an alternative by taking a contractarian perspective, according to which social arrangements should not be assessed from the viewpoint of an impartial and benevolent social planner but from the viewpoints of the individual members of the society that is being assessed. The principle of the contractarian perspective is that it does not ask whether aggregate welfare is maximised, but whether it is in the interest of each individual to accept the rules of that institution, on the condition that everyone else does the same. The particularity of the contractarian recommendation is that it is about the good of each one, not about the good of the whole.

The second target of Sugden's criticism is developed in Chapter 4, where he challenges the consensual assumption of behavioural welfare economics that individuals have true preferences. The main argument is that there is no existing psychological justification for the view that individuals, in the absence of errors of reasoning, have the ability to reveal their "true" preferences which appear to satisfy the axioms of rational choice theory. In the absence of a solid argument for the construction of the concept of true preference, Sugden argues that normative economics must adapt to human psychology as it really is. This means that it should not take individuals as making "wrong" decisions but instead develop an approach compatible with their preferences as they really are.

Having tackled two important characteristics of behavioural welfare economics—that it takes the "view from nowhere" and assumes that individuals have underlying true preferences—the next four chapters aim at reconstructing normative economics without the concept of preference. Chapter 5 proposes an alternative direction for normative economics that substitutes the criterion of preference-satisfaction with the criterion of opportunity. According to Sugden's opportunity criterion, it is good to provide individuals with more

[1] With "the view from nowhere", Sugden updates the criticism of Buchanan (1954) toward standard welfare economics. The point of Buchanan was that the concept of "social preference" makes no sense because the society is not a person, and therefore cannot be attributed a "preference".

opportunities to choose rather than less, regardless of what their preferences turn out to be. This normative criterion represents the interests of individuals viewed as responsible agents, such that at each moment they identify themselves with their own past, present and future actions. The concept of responsibility is central in Sugden's opportunity criterion as it provides a philosophical underpinning for the claim that opportunity has value in itself.

Chapter 6 identifies the conditions under which the competitive market provides opportunities and explains how these properties can be seen as beneficial when individuals do not specifically act on well-ordered preferences. Sugden proposes a general equilibrium model, in which he demonstrates that in every competitive equilibrium, individuals' opportunity sets satisfy a condition that he calls the "Strong Interactive Opportunity Criterion" (118). This condition requires that individuals collectively have the opportunity to make any feasible transaction among themselves which they might find mutually acceptable. Sugden interprets this property of markets through the invisible hand of Adam Smith's *Wealth of Nations* and argues that its validity does not depend on rational choice theory.

Chapter 7 asks what role government regulation can play in helping to provide individuals with opportunities for mutually beneficial cooperation. After a review of the neoclassical arguments for regulation, Sugden discusses two potential psychological criticisms of his opportunity criterion: consumers may face "too many" options so that the quality of their decisions declines (choice overload); and consumers may want to constrain their own opportunities (self-constraint). He then provides regulatory responses to the problem of firms that deliberately price or present information about prices in unnecessarily complex ways (obfuscation); to the problem of fixed costs and price discrimination (natural monopoly); and to the problem of public goods.

Chapter 8 considers what properties a market economy needs to have so that its governing principles are psychologically stable when viewed from a contractarian perspective. The concept of psychological stability is defined along the lines of Rawls' *Theory of Justice*, namely that "if a conception of justice is to be public, the hypothesis that individuals accept its principles must be consistent with the facts of human psychology." (174) By criticising the theories of justice of Dworkin, Cohen and Roemer, Sugden argues that there is a tension between the idea of a fair baseline and the principles by which real market economies work. Consequently, he upholds that psychological stability must rest on continuing expectations of mutual benefit: each individual citizen who seeks his/her own interest agrees to conduct his/her economic affairs in the expectation that those terms will have continuing psychological stability.[2]

The last three chapters of Sugden's book provide an understanding of the moral status of market relationships. Chapter 9 aims at understanding the practices of reciprocity. The author argues that the kinds of pro-sociality that allow individuals to solve collective action problems are not antithetical to the motivations by which people realise mutual benefit in markets. Sugden first criticises two different kinds of literature in virtue ethics (Anderson, 1993; Sandel, 2009) and behavioural economics (Pelligra, 2005; Rabin, 1993) that he considers providing erroneous representations of market relationships. He then proposes an original understanding of reciprocity as a mutually beneficial cooperation. This principle is based on a theory of social norm, which, in contrast to the one of Bicchieri (2006), does not distinguish a social norm from a moral rule.

Chapter 10 proposes a model of pro-social behaviour where market transactions are not fundamentally different from cooperative activities in other domains of social life. Sugden's analysis of team reasoning accounts for practices that individuals follow in market interactions. He defines these practices as social norms that have already been established and that most individuals tend to follow. After identifying the conditions under which interactions can be understood as voluntary, Sugden explains what it means to intend mutual benefit in a voluntary transaction and illustrates this intention with four examples of games involving reciprocity. He argues that reciprocity is best explained by individuals conforming to ongoing practices that allow them to realise mutual benefit.

In Chapter 11 Sugden provides a philosophical definition of the principle of mutual benefit. The particularity of this final chapter is that the author explicitly addresses his "real fellow-citizens, not the imaginary individuals of a theoretical model." (262) He defines the principle of mutual benefit as a psychological process similar to the particular sentiment of sympathy in Smith's *Theory of Moral Sentiments*, arguing that the sympathy of fellow-feeling is what psychologists now call emotion contagion—a phenomenon recognised by empirical evidence in neuroscience. In conclusion, the book provides an

[2] In Chapter 8, Sugden relies heavily on Hayek (1948)'s criticism of market socialism, according to which the dynamic process by which equilibrium is reached is not taken into account. Like Hayek, Sugden claims that the dispersed knowledge of individuals and its combination is essential to understand the mechanism of the market. Although Sugden refers to Hayek exclusively in his eighth chapter, a reader who is familiar with the liberal tradition can perceive the general influence of Hayek on Sugden's arguments throughout the book. For example, his view that the preferences of consumers determine the production of goods and services and his view that each individual is responsible for his own choices can relate to the term "consumer sovereignty", which is never mentioned in the book.

understanding of the market viewed from the viewpoint of virtue ethics: if virtue ethics theory needs to attribute a function to each domain of life, the telos of the market is mutual benefit.

The Community of Advantage is a masterful book that brilliantly articulates behavioural economics, welfare economics, social choice, theories of justice, philosophy of economics, history of economic thought, political philosophy and moral philosophy into a unified system that shapes the grounds for an alternative form of normative economics that does not require the concept of preference—a concept that has been central to welfare economics since its beginnings. The book is extremely skilful: it combines empirical findings of experimental economics, high-level theoretical modelling and consistent philosophical and historical backgrounds. Regarding its massive contribution and its dense content, the book is impressively concise (296 pages when counting the eleven chapters and their footnotes) and uses technical modelling only when necessary. As the range of subjects tackled by the author in his attempt to reconstruct normative economics is vast, there is a chance that many pro-market positions remarkably defended by the author will be subject to vigorous debates in the next few years across several rival positions to Sugden's, such as welfarism, paternalism and egalitarianism. In the following sections, I provide two comments on (1) Sugden's answers to the potential psychological criticisms of his opportunity criterion and on (2) Sugden's overall aim of convincing the reader of the value of mutual benefit, but not showing that mutual benefit is what economic transactions actually are.

2. Limits of the Opportunity Criterion

Sugden discusses two potential criticisms of providing individuals with more opportunity to choose, based on two psychological traits: consumers may face "too many" options so that the quality of their decisions declines (choice overload); and consumers may want to constrain their own opportunities (self-constraint).

Sugden's discussion of choice overload addresses Schwartz's (2004) book about the harmful psychological effects of having more choice than less. Sugden's concern is whether more opportunities to choose has indeed a negative impact on individuals' well-being, and if it is so, to what extent. He gives two arguments against choice overload. The first is that in situations where individuals know what they want, more opportunity to choose is better than less since individuals will more likely find what they are looking for. The second is that when goods are categorised (e.g. varieties of tea and coffee are classified in different sections in the supermarket), individuals have less trouble making their decision since categorisation makes the range of goods more easily comparable. There may be however some persisting issues when using these two arguments, particularly when we confront Sugden's view to other behavioural studies that do not underline that individuals most of the time know what they want nor that most of the goods in the economy can often be as easily categorised as in the supermarket.

Firstly, it can be argued that in many cases individuals merely do not know what they want. An important psychological trait identified by Baumeister (2003) is that the more decisions there are, the higher is the cost of thinking about each decision. A question then worth being asked is to what extent the market is a good environment for learning what individuals want. In cases where commodities are not new, consumption habits can produce a kind of knowledge that leave individuals unaffected by choice overload—e.g. someone may find many different types of bread in a bakery; yet being familiar enough with the taste of each bread he/she has no trouble knowing the bread he/she wants. But in other cases where commodities are new, it may take some time and effort for someone to know whether he/she wants a certain good. An example of a market which is surely exposed to uncertainty of knowledge is information technology—e.g. it may take a while for someone who is already in possession of a smartphone and a laptop to decide whether he/she wants a tablet. One answer in the case of markets that are prone to uncertainty of knowledge (such as information technology) is that by providing more opportunities for everything, the market can also provide more opportunities for learning and create businesses of categorising information about products such as online comparators of holiday trips, flights or types of insurance. Such markets of categorisation may eventually help consumers to make decisions on products that they would not have been able to do otherwise. Still, this does not seem to solve the initial problem of choice overload: if there are many opportunities for choice, there may then be more opportunities for categorisation and eventually a bigger range of comparators—e.g. Kayak, Edreams, Gotogate, Jetcost, Liligo and Skyscanner in the market of flight comparators—but that would leave the consumer no better off, knowing that they have a limited ability of treating the information.[3]

Although the following term is never used by Sugden, the idea of the opportunity criterion is to maximise the range of opportunities to

[3] A way out of this vicious circle may be to add to the opportunity criterion a form of the concept of satisficing (Simon, 1956). The concept of satisficing explains the behaviour of a decision-maker in situations where an optimal choice cannot be determined, mainly because his/her information and ability to treat the information are limited. In the case of choice overload, we may presume that individuals will stop the search at a satisfaction level that fulfils all of their needs. This point could potentially lead to fruitful research (if it does not already exist) regarding how the two normative concepts of opportunity and satisficing can be joined together in order to improve normative analysis.

choose. Of course, firms may take into consideration cognitive limitations of individuals in order to avoid some negative effects of choice overload on their businesses. For example, if consumers cannot "make up their mind" and end up choosing nothing, it would make no sense to propose "too many" goods in the supermarket. Along this line, there may exist a limit beyond which individuals cannot be provided "too many" goods (for the interests of consumers and firms); hence the need to set a range of choice opportunities that does not exceed this limit. But setting such a limit is contrary to the principle of Sugden's opportunity criterion that does not foresee a limit of the domain of opportunities for choice. One answer we can find in Sugden's idea of market transactions as mutually advantageous is that it will be unlikely that markets where individuals are given "too many" opportunities to choose will be sustainable in the long run, because if individuals do not consume in these markets, some businesses will simply cease to exist. The reader may, however, have good reason to dispute this point of view. In economic theory we reasonably assume that consumer taste is the major factor that determines how the market economy is ruled. As an example, Sugden (144) asks why businesses such as Walmart and Amazon, which provide a huge opportunity for choice, are so successful. But in reality, there are important factors other than individual taste that strongly influence consumption on an aggregate scale. Two of them are that what others consume influences each individual's consumption (social trend or mimetism); and that firms influence what individuals consume through advertising and framing effects.[4] If we consider that individuals' ability to treat the information could in some way be given normative significance and if we do not follow Sugden's implicit theory of how businesses are sustained in the real economy, we can object to Sugden these two limits to his opportunity criterion. It distances itself from human psychology as it really is—what he initially criticises in the true preference criterion. It distances itself from the way the economy is ruled beyond forces at the individual scale—while Sugden specifically argues that one major aspect of economic reality is the desire of individuals for more opportunities to choose.

The phenomenon that firms deliberately price their products, or present information on prices, in unnecessarily complex ways (obfuscation) and the case of market oligopolies (particularly natural monopolies) are well recognised by Sugden in Chapter 7 where he provides answers to how markets can be regulated when consumers lack well-ordered preferences. But his answers may still appear unsatisfy-

[4] The economic literature which introduced the quality of the goods and advertising as economic variables (Chamberlain, 1953) is worth being discussed here. For the importance of a better conceptualisation of goods and a better understanding of how market participants perceive goods as similar or different, see Dekker and Kuchař (2016).

ing to account for the limited ability of consumers to treat information if we carefully look at the way the range of goods are actually categorised in the economy. In a recent study, Heidhues, Johnen and Köszegi (2018) explicitly differentiate between goods that are easily categorised in real-life situations—such as products in the supermarket—and other goods that are not categorised—such as phone contracts, credit cards or mortgages—that consequently demand cognitive efforts from consumers in order to choose the product that satisfies their wants. The authors emphasise two types of behaviour that result from these two types of goods: choosing quickly but superficially (browsing) or choosing carefully but slowly (studying). Contrary to Sugden's approach, they start from the fact that many market domains are already regulated, such as water, food and electronic products. An important question they raise is what would happen if these goods were not regulated. Their answer is that individuals would have to "study" to make sure the goods fit their initial wants, meaning that they would not be able to compare as many products as they would like to, which eventually would lead to a fall of market competition. In other words, their study yields to an argument for regulation in favour of market competition. Contrary to the liberal view of economics which states that regulation normally induces market inefficiency because consumers cannot buy what they want, their paper argues the opposite: regulation helps individuals to compare goods, which consequently increases market competition.

The second psychological limit to Sugden's opportunity criterion concerns situations in which individuals want to constrain their own opportunities for choice. Taking Sugden's example (150), consider an individual called Jane who has two possible consumption options *fruit* and *cake* that she can consume in periods 1 and 2. Since she can choose between a fruit and a cake in both periods, her opportunity set is defined as O = {{*fruit*, *cake*}, {*fruit*, *cake*}}. Now assume a different scenario in which Jane, for personal reasons, would like to constrain her own opportunity set to only *fruit* in period 2. Since she can choose between a fruit and a cake in period 1 but only a fruit in period 2, her opportunity set is defined as O′ = {{*fruit*, *cake*}, {*fruit*}}. According to Sugden's individual opportunity criterion—which states that any expansion of a person's opportunity set promotes her interests—O dominates O′. However, if we follow the classic liberal argument that we must give fundamental importance to Jane's choice because it is her choice, we must respect her will to restrict her freedom to choose and therefore rank her opportunity sets in such a way that O′ dominates O. Clearly, the opportunity criterion suffers from a paradox in situations of self-constraint: it cannot account for the interests of individuals who want to constrain their own options without violating its principle of providing individuals with more choices. This limitation is acknowledged by Sugden, who notes that,

> How far a regime of voluntary transactions should be regulated so as to support individuals in imposing constraints on themselves is a deep problem that generations of economists have struggled with. I can only say that my analysis, as I have so far developed it, abstracts from this problem. (151)

His main defence is to maintain that few domains of economic reality involve situations of self-constraint, making the latter of marginal importance. Even if many will probably agree with Sugden that self-constraint is not frequent in markets, it remains, on principle, an important objection to the opportunity criterion. This objection also raises the question of how seriously behavioural economists should take into account the liberal view that individuals are the best judges of knowing what is best for themselves. As Sugden does not discuss this point, his reconstruction of normative economics rules out decisions of addictive, childish or mental disorder attitudes that presumably do not reflect what is best for these categories of individuals.

3. Rescuing the Liberal Tradition of Economics

My second comment concerns Sugden's general attempt to maintain the liberal tradition of economics against forms of paternalism that derive from behavioural economics which are, in his words, "appealing to a sensibility that is hostile to principles of economic freedom [which] for two and a half centuries, have been central to the liberal tradition of economics." (x) It may firstly be disturbing to some to see how Sugden's reading of Smith and Mill throughout the book is taken to support his liberal defence of the market. While the *Wealth of Nations* and *On Liberty* were written on the subject of the limits of the power which can legitimately be exercised by the State over the individual, both of these early writings gave a relatively strong power to the State to regulate market competition, showing that many markets could not be overtaken by private firms. If one has a different reading of Smith and Mill than the liberal perspective presented by Sugden, one will not share Sugden's views on the invisible hand and the market for mutual advantage—two concepts extracted from two thoughts that were far from embedded in the modern conception of liberalism. Knowing that Smith and Mill did support many interventionist policies, one may ask whether their thoughts could not put forward interventionist/regulatory policies that Sugden would be opposed to, such as limiting the sets of opportunity. Even if the strength and validity of Sugden's arguments ultimately do not depend on whether his reading of Smith, Mill and other early authors is correct, some interpretations of Sugden's positions may nonetheless be subject to debate—for example, that Hume's theory of conventions follows a contractarian approach (34) or that the two theorems of welfare economics represent the idea of *The Wealth of Nations*' invisible hand (107).

More importantly, this is not to say that normative economics and the liberal tradition should be maintained together at all costs because principles of economic freedom have always been central to the liberal tradition of economics. Sugden shows that normative economics has no particular reason to continue with the concept of preference. One could also question whether normative economics has any particular reason to continue with the liberal tradition at its basis. Despite the clarity of the book, a point left unclear in Sugden's attempt to defend the competitive market as a place for mutual advantage is whether he puts forward his liberal arguments based on what the market *actually does*, or on what he *wishes* the market to be. This confusion particularly appears in his ultimate chapter where he acknowledges that he does not take the social interactions analysed in the book to be the way every economic interaction actually works, but that he tries to "persuade" (256) and "convince" (281) the reader that a morality of mutual benefit is an appealing view of how we could see social interactions. One question the reader may ask is whether Sugden's whole project of reconstructing normative economics does not reverse the main approach to normative analysis that is commonly found in behavioural economics. While behavioural welfare economics can derive policy recommendations from the explanation of human behaviour, it is not entirely clear whether Sugden gives more importance to how economic reality is (arguments he puts forward in Chapter 7 and Chapter 8) or how we could see the market economy (arguments he puts forward in Chapter 11). To put it differently, is it the view of what the market really does, or what it could do that led Sugden to propose his form of normative economics? This question is worth being asked by all those who are not convinced that a political stance could play a special role in reconstructing normative economics, but who believe that the behavioural paradigm could be informative toward which policy (e.g. liberalism, interventionism or paternalism) to adopt. The documentation of cognitive biases was initially the main reason why eminent behavioural economists such as Daniel Kahneman and Richard Thaler tried to rely on psychological principles (hedonic states and true preferences) in order to represent individuals' well-being. Being aware of the two extremely important objections to the assumption of individuals having true preferences and to the "view from nowhere" that Sugden exposes, the psychological traits of choice overload and self-constraint previously discussed remain two examples of insights being legitimately informative about which policy (e.g. a more liberal or a more interventionist one) could be adopted.

My point is: rather than justifying a normative criterion from a general principle such as freedom to choose, a general principle such as freedom to choose could be the by-product of the endeavour to find an appealing normative criterion that could successfully lead to a consensus about what matters to individuals. In other words, political stances such as liberalism, interventionism or protectionism should not be given any a priori importance (what Sugden seems to do with liberalism) but instead be the result of which kind of policy we have reason to apply after careful investigation of how individuals make decisions.[5]

4. Concluding Remarks

Although the liberal arguments that follow from Sugden's contractarian approach and opportunity criterion may not convince everyone, *The Community of Advantage* will without doubt become a major reference to every researcher interested in the current difficulties of finding a normative approach consistent with behavioural economics. As behavioural welfare economics is presently the mainstream approach to normative economics in the behavioural paradigm, it is important to have a leading figure in behavioural economics such as Robert Sugden to show that an alternative direction is possible, even if one's main interest in the problem of reconciling normative with behavioural economics is unrelated to the aim of preserving the liberal tradition of economics. Sugden's book will leave no scholar in normative economics indifferent as to how he sees the competitive market as a place for mutual advantage. This book will undoubtedly nurture researchers having a strong interest in providing solutions for important issues in welfare economics and/or social choice—probably one of the most important issue being the difficult challenge of finding a normative criterion that is both consistent with the findings of behavioural economics and liberty-preserving.

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[5] This last point may, of course, fall back on a form of the Hume's guillotine (inferring an *ought* from an *is*) that could be bypassed using e.g. a reasonability category proposed by Sen (2017 [1970], Chap. 5). Such a philosophical justification goes however beyond the scope of this review essay.

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