

Module 2

Lecture 11

Topics

2.8 Mill's approach to economics

2.9 Mill on social policies: Laissez Faire or Socialism?

2.10 Mill's Value theory

2.8 Mill's approach to economics:

- J.S. Mill's views on economics are well represented in an article published in 1836 and in his Principles published in 1948.
- His position on the methodology of economics is a divergence from mathematical abstraction that Ricardo advocated. He did not completely reject the deductive method used by the economists where result was derived on the basis of abstract models. But he cautioned against relying too much on the predictions of such models. He was critical about accepting the deductive model simply because it is not possible for the social scientists to run controlled experiments. Therefore, he advised to match the prediction of a model with moments in the history.
- A mismatch between the prediction by the deductive models and historical facts will point to "disturbing causes" which will improve the theory. In a sense he was more Smithian than Ricardian as he embraced contextual theory in place abstract, deductive models. Even if he admitted that the assumption of rational agent -- whose sole motive is to acquire as much wealth as possible -- produced some useful results in economics, he strongly believed that human behavior can be better understood using an inter-disciplinary approach consisting of different social sciences.
- Mill maintained that his single most contribution is making the distinction between the laws of production and the laws of distribution. The laws of production, according to Mill, are the same as the natural law – beyond the scope of human beings to change them. The laws of distribution are social construct and can be

changed through political processes such as trade union movements or income redistribution process. He was critical of the economists who thought none of the laws can be changed. He maintained that only the laws of production are more or less fixed.

- It logically follows from his position that there is no need for the wage to be fixed at the subsistence level as Ricardo predicted. The wage is determined through a bargaining process which depends on the social and political institutions. He believed that taxation can be one instrument of bringing equality. He favored tax of inheritance but opposed progressive taxation in the fear that it might provide disincentive against business proliferation. However, modern orthodox economics does not see these two laws as orthogonal to each other as viewed by Mill. The law of production is labeled as the production function which is not completely exogenous to different social parameters. However, in static analysis in orthodox economics, production function is largely considered as exogenous.

2.9 Mill on social policies: Laissez Faire or Socialism?

- Mill in his methodology followed eclecticism drawing upon different methodologies. This also reflected in his policy prescriptions which were somewhere between classical liberalism and socialism. His brand of socialism was far from Marxism and between his own classification of revolutionary socialism and philosophical socialism -- his theories were closer to the latter.
- In his essay *On Liberty* (1859), Mill tried to elaborate his view of the ideal relationship between government and the people. He belonged to the school of classical liberalism which allows people to do whatever they want as long it does not harm others. According to Mill, government should intervene if one's free will action harms another person. However, while discussing social actions he abandoned strong liberalism in favor of making exception to achieve great good. He supported laissez faire as a general rule but made room for government intervention if need arises. In a way, he stops short of the nihilist agenda – abolition of the government and acknowledged that the absence of government does not always imply maximum freedom.
- Mill, like other classical political economists, talked about class conflicts. Following Ricardo and Smith, Mill was also critical of the landlords and maintained the position that they don't have any ethical right on rent as the landlords have not contributed anything to the production of grains. Building on Ricardo's rent theory, Mill perceived class conflict between landlords and the rest

of the society. However, he never predicted any class conflict between labor and the capitalist classes. This is surprising given that Mill strongly advocated redistribution in favor of the poor, universal education, the shortening of working day. All this policy suggestions recognizes the political antagonism between the labor and the capitalist classes even though Mill never formally admitted it.

- Mill's view on private property is a blend of classical liberalism and social reform. He did not recognize the right to private property as a sacred cow which can never be compromised. For him, private property right is not absolute and can be altered if society finds that suitable. He in fact discussed communism as an alternative system but preferred private property based regime to communism.

2.10 Mill's Value theory

- We already have discussed that Mill's economics methodology was a mixture of Ricardian abstraction and Smithian contextualization. Here we discuss his most significant contribution: value theory.
- Mill's theory of value or relative prices was a rejection of Ricardian theory.
- Mill gave up the Ricardian search for absolute value based on some invariant measure of value and took the position that the purpose of value theory is to explain relative prices. He realized that the opportunity cost of land is not always zero and rent can enter as a social cost of production whenever there are alternative uses of land.
- He did not explicitly formulate the demand and supply theories but his notion of relative price determination used these concepts.
- According to Mill, for a good to have exchange value or price, it must be useful and difficult to obtain. He argued that there are three groups of goods where the demand and the supply play different roles in determining the prices. Remember, that Mill did not use the concepts of demand and supply curve. But his argument essentially captured the demand and supply curve based argument. However, while elaborating his point we use terms such as demand and supply to make the point clear.
- In the first group, where the supply is limited, (e.g. painting, antique goods, rare books) price is determined by both demand and supply.

- Mill argued that the second group of commodities, manufacturing goods, has perfectly elastic (horizontal) supply curve meaning that they are produced under the condition of constant cost. Hence, price is completely determined by the cost of production and independent of demand.
- The third group, agriculture, according to Mill has an increasing marginal cost curve. He implicitly assumed diminishing return in agriculture which would result in upward sloping supply curve. This means that price is determined by both demand and supply.
- Even though, Mills did not discuss these theories explicitly using demand and supply curves or mathematical equations. But his arguments formed the basis of neo-classical theories which emerged 50-60- years after Mill's scholarly work.